PROBLEMS OF RESOURCE MOBILISATION IN THE STATES

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CONFERENCE PROCEEDINGS

April 21, 1969

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FOREWORD

It is agreed on all hands that mobilisation of resources is a *sine qua non* for planned development of the economy. With all the infrastructure provided, economic growth should itself function as a feed-back mechanism with more and more production, yielding greater and greater resources for being ploughed back into the diversifying economy. Even at the best of times, resources mobilisation is a daunting proposition. In a poor country like ours, it is tied up with the political will to act and get things done, within the tolerance of a functioning democracy. In a federal structure these tolerances are narrow and even forbidding. The innovating character of the political experiences we have been going through since the last general elections, merely adds to the complexity of the situation.

It is in this context that the Conference on Problems of Resource Mobilisation in the States took place earlier this year. The fifth Finance Commission has reported since then its findings and recommendations. The Government of India have already implemented those relating to the sharing of income-tax, Union excise duties and additional duties of excise in lieu of State sales-tax and payment of grants-in-aid of the revenues of certain States under Article 275 (1) of the Constitution. The Commission's several suggestions in regard to the scope for raising revenues by the States are still under consideration of the Central and State Governments.

Various State Governments have set up their own Taxation Enquiry Committees to sort out the problems of resources mobilisation for themselves. I am glad to say that one of my colleagues, Dr. M. J. K. Thavaraj, Professor of Financial Administration has been actively associated with some of these Committees.

The IIPA, recently organised the Conference on Problems of Resource Mobilisation in the States largely on Prof. Thavaraj's initiative. In view of the importance of the subject, we feel that it would be useful for the public to let them know

the views expressed and comments on the subject held by administrators and other public men. The proceedings have been carefully edited by Prof. Thavaraj who was assisted in his labours by Shri K. B. Iyer, our Training Associate.

I do hope that this study of Centre-State financial relations and problems of resources mobilisation will interest the administrators, the politicians and the lay public.

J.N. KHOSLA
Director
Indian Institute of
Public Administration

NEW DELHI
November 25, 1969

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WELCOME SPEECH

J. N. Khosla

Professor Gadgil and distinguished guests, I consider it a great privilege to welcome you all on behalf of the Indian Institute of Public Administration and on my own behalf. You have been good enough to come to this Conference to discuss one of the most important problems which is exercising the minds of the planners in India at the present moment. In the National Development Council which met yesterday and the day before, the Prime Minister had focussed attention on the seriousness of the problem of resource mobilisation in the context of the Fourth Five Year Plan. She made a particular reference to the fact that taxation as a percentage of national income has registered a decline from 14.2 per cent in 1965-66 to 12.3 per cent in 1967-68. We are aware that taxating is an unpleasant job and all popular governments would like to keep it within tolerable limits and yet, without substantial domestic mobilisation neither self-reliance nor rapid economic development is possible. As Vice-Chairman of the Planning Commission, you, Sir, are aware of the resource bottlenecks which seriously constrain the implementation of plans both at the Centre and in the States. In a backward country such as ours where more than three quarters of the population live below the subsistence level of income, we cannot possibly get away from the dilemma arising from the simultaneous pursuit of the objectives of rapid development and reduction of inequalities in income and wealth. Yet restricting resource mobilisation to areas where surpluses occur would unduly restrict the tax base. It is particularly difficult in a mixed economy where surpluses mopped up by the State are likely to create disincentive effects on investment and production. This is as much true of the agricultural sector in the States as in the corporate sector which is the concern of the Central Government. I hope this Conference would identify some of the

constraints that operate on the resource raising capabilities of the States and suggest ways and means of removing them.

As a student of political science and international affairs, I am not aware of any federation in the world today which is free from conflicts between the different layers of government. It has been there in the Indian Union ever since it became a Republic. But most of these conflicts could not manifest themselves before the public owing to the towering personality of Pandit Jawaharlal Nehru as well as to the reasonable political homogeneity that characterised State Governments before the last general elections. It may also be borne in mind that the nature of the Indian Union could have been different had it not been for the partition and the impulses and misgivings which it gave rise to. It may be that the unity of the Indian Union depends on some basic readjustments in Centre-State relations of which financial relations is an important aspect. May be the Conference could contribute materially in suggesting ways and means of resolving these conflicts.

Ever since the separation of Burma from India, food problem has stayed with us. The partition of India had only aggravated it. Despite our emphasis on rapid industrialisation of the economy, we have directed considerable resources for the development of agriculture. Yet all the studies indicate that its contribution to the exchequer is not commensurate with what it has got out of it. It is understandable that when we are preoccupied with the task of enlargement of our food baskets we cannot throw undue burdens on the millions of our peasants. At the same time it stands to reason that the upper strata of the farmers who happen to be the largest beneficiaries of our subsidised inputs and investments should be tapped more intensively as part of the mobilisation efforts of the States. I hope the Conference would pay adequate attention to the problem of resource mobilisation from agriculture.

The Institute is always eager to focus attention on current problems of national importance. We are indeed happy to have taken advantage of the presence of most of you in Delhi in connection with the National Development Council meeting. As you are aware, Dr. Thavaraj, one of my senior colleagues in the Institute, was the Chairman of the Taxation Enquiry

Committee, Government of Kerala. It is due to his imagination and initiative that this Conference was made possible. I would like to express my warm appreciation for the good work he has done. Along with a paper which the Planning Commission had prepared on Resource Mobilisation in Agriculture, we had circulated a few chapters relevant for discussion in this Conference out of the Report of the Kerala Taxation Committee. We are very much aware that what is applicable to Kerala may not always be good for other States. The economic situations, political complexions, geographic and climatic variations and so on would suggest different approaches and solutions to the mobilisation problem. But I hope that these papers along with the working paper would provide the basic material for the Conference.

I extend to you my heartiest welcome. Most of the participants of this Conference have also been actively involved in the proceedings of the NDC in some capacity or other in the last two days. We really appreciate that you were able to spare one more day to enrich the proceedings of this Conference.

May I welcome you all and thank you for joining us at this session ?

INAUGURAL SPEECH

D. R. Gadgil

Dr. Khosla and friends, I am indeed very glad to be here this morning. As Dr. Khosla has pointed out, this is a subject of crucial importance relating to the work of the particular office which I happen to hold for the last year and a half. Therefore, whatever may have happened in the recent past, looking to the future of planned development in India, I think this is a subject of the greatest importance and it was a very good idea on the part of the Institute to take advantage of the presence in Delhi of number of important people interested in the subject and associated with its consideration for this particular Conference.

I am not quite sure that I can contribute anything very significant to the deliberations of a body composed of persons as well-informed and as fully aware in relation to practical details as well as to the theory of the problems involved, as are assembled here today. However, I will permit myself to making a few general and specific observations which, I hope, would be taken up in later discussions.

I assume that you shall be discussing the problem of resource mobilisation for planned economic development in the country within the federal structure and in the context of the division of resources and other arrangements like the working of the Finance Commission incorporated in the Constitution. This apart, the State is looked upon as the initiator, organiser as well as the regulator of crucial economic activity and this role of the State is related to planned economic development. There is also an assumption about the minimum of total national development that is needed. All this calls for a transfer of resources from private to public hands and the main problem you are confronted with is how this transfer is to be brought

about—from what categories, classes, in what manner and how effective and intelligent its uses in public hands ought to be. It may be borne in mind that no State by itself can pursue an independent development programme, which is bound to result in considerable variations in the projects of the different States as amongst themselves on the one hand and between the Centre and the States on the other, leading may be to retardation of development rather than acceleration. It will be appreciated, therefore, that a certain minimum of preparation in development planning is an essential part of the working of the federal organisation. These are all obvious things and I am sure you are well aware of the same. But I believe sometimes it is necessary to underline even the obvious things in a discussion of this character.

The Constitution delineates the division of resources as between the Centre and the States and the division of responsibility in terms particularly of development planning as between the Centre and the States. But it did not envisage the dichotomy between the Plan and non-Plan outlay—the role of the Planning Commission, and the role of the Finance Commission. You are also aware of the great accumulation of debts—debts in relation to Plan outlays, debts for other kinds of special purposes, *ad hoc* loans and so forth as between the Centre and the States and you are aware of the totality of the situation which you are dealing with today.

You are thinking of additional resource mobilisation. The term 'resource mobilisation' covers much more than taxation. It covers the income from public services, public enterprises and public utilities. All this is a part of resource mobilisation which is open to the States. As for taxation, I would draw your attention to the fact that the base of State resource mobilisation is not as narrow as is sometimes talked about. All taxation on agriculture including income tax on agriculture is outside the purview of the Union Government. If you develop agriculture then the base is not narrow and if the States have the will, there is considerable leeway in terms of resources that they can make up in this direction. I am sure you will all go into the problems of land revenue reform. Land revenue reform is being talked about for decades. One of my first

pamphlets as an economist written in 1927 involved a debate in the Bombay State regarding the old land revenue reform. The position has remained the same even after the Report of the Taxation Enquiry Commission. The effort involved and the whole series of the complications—theoretical, practical and political—in land revenue reform are such that both theoretical and practical persons would agree that we may as well let the system remain in most of the States and let them tackle it in their own way.

As a matter of fact if you look at the history of State taxation in the agricultural sector during the last decade you will find that agricultural income tax has neither been taken seriously nor pursued rigorously or logically anywhere. All other kinds of taxes, such as taxes on cash crops, market charges and so on have been thought of. But taxation on agricultural income remains much neglected.

There is no use dodging this question of mobilising more resources from the growing agricultural sector. It may be dodged for another one or two elections. But it may be found very difficult to bet beyond that. I am hopeful that with planning, agricultural development would be stepped up as indeed it has been during the last few years. When this happens the urgency of taxation of agricultural incomes will be felt increasingly. I think there is no other logical way of taxing this sector except through income tax. From the point of view of national policy it is also logical and economical to pool the agricultural and non-agricultural incomes together for purposes of taxation. When in 1947 the draft Constitution was being framed, I urged the Constitution-makers not to put agricultural income tax in the state sector. It is an inheritance from the middle of the 19th century when the income tax was first introduced by the British. There was land revenue which was very good. The income tax was introduced as an urban tax. The Constitution was made in the middle of the 20th century and the 19th century concept was all wrong. I hope that the State Governments will soon agree to some kind of adjustment by legislation and so on, so that there should be one unified income tax. The loss in not doing so is very apparent for all sections of the people including the States. The loss to the States is very great. For

instance, in Maharashtra the proceeds from agricultural income tax are only Rs. 30,000 to 36,000. It is not that you lack resources. The resources are there. It is criminal not to mop up the surpluses from sugarcane farming. I note that a large bulk of the audience and the participants are officials and I am not expecting them to speak out in any manner as I could. But I am sure the officials will appreciate somebody like me to put across, whatever, may be the political difficulties, these things in an outspoken manner.

Take the idea of rural debentures. I mention this because of certain experience I have, for example, in Maharashtra State, regarding rural debentures for land development banks. It was possible, two years ago for the Maharashtra cooperatives, with the help of State Cooperative Banks, to put up a scheme of inter-factory lending, together with bank lending so that necessary finances were available. Now that it was possible shows that there are funds waiting to be mopped up. This I want to underline. The Planning Commission has put out this idea of rural debenture largely because we know that in the present context, direct tackling of agricultural income is not quite possible. This is not a good situation for development planning in India. The desirable situation is where everybody contributes so that there is general development. The idea of the rural debenture will be confined to certain areas, or certain sectors. This will create imbalances between classes and so forth. It only makes it possible for channelising these surpluses in given areas.

Now let me go on to the field of property taxation and land taxation—urban property taxation as well as rural property and land taxation. Land use policy includes land acquisition, land taxation and regulation of land prices and land uses especially in the development of metropolitan areas. I hope, all of you realise how important it is that metropolitan development should be self-financing. If the largest areas of surplus have to depend on some body else—and quite obviously there is nobody else who can contribute—these areas must raise funds for their own development and this can only be done if you have a land policy and a proper taxation policy. This is a question of State taxation, local taxation and it is one of the matters with the local

authorities. But I want to emphasise the need for State Governments to look into property taxation and urban land problem. This is also of special importance in areas where agricultural development is proceeding apace, and land values are increasing in rural areas.

Another important problem which comes to my mind is the extent to which we have resources to be put into particular type of development. For instance, in the context of urban development, housing is very important and we have had through the plans, a large number of miscellaneous programmes of rural and urban housing. If you look carefully at the amount of allocation for housing, it is absolutely insignificant in relation to the total requirements. If you look at the magnitude of the problem you will find that the provision of housing through public expenditure is almost impossible.

In public housing, a factor which cannot be overlooked either by the Central Government or the State Government or the Planning Commission, is the wide divergence in standards of urban and rural housing, the former bearing no relation to the living conditions of the vast majority. Conforming to the present standards of urban housing, rural housing being substandard, current levels of outlay could provide housing for only a small number of people. Since public housing touches only the fringe of the problem, we have to think in terms of private, cooperative and other efforts in housing. If that happens, you will get this question of land acquisition; zoning and land use and so on become important even in quickly growing villages. I do not know how many of you are acquainted with the areas where insanitary conditions are rapidly growing today. I am particularly referring to the insanitary conditions in the villages; they are worse than some of the towns. More and more people are coming; the original sanitary, road, drainage conveniences are scanty or non-existent. Land prices also go up. At the moment there is very little concern for these problems. But these are important problems to which the State and local authorities should address themselves. In view of this, the State and local governments would do well by tapping property, either of building or land, which are fully within their powers.

I would also like to draw your attention to a few other sources.

Let us take up octroi and tolls. In my view toll is unnecessarily neglected in India. It is quite true that for some reasons octroi has been objected to, theoretically and otherwise. We have not abolished octroi, though we have had to do away with it substantially. On the other hand a toll on bridges, for instance, is an extremely important source which might be exploited. From what the reports say, response to the lottery is quite enthusiastic. I do not know how long it may sustain. I do not know whether it is good or bad. But it has become a new source of mobilisation. It is a kind of saving effort. In a State-run lottery, the aspect of saving or provident fund can be associated with the element of a speculative gain. You may discuss these aspects.

The last point, I would like to refer, relates to the incomes from public sector enterprises and utility services. Here again, we have not thought out our ideas fairly clearly. The old concept with which we began during the war time, *i.e.*, going in for State trading on a no-profit no-loss basis is still lurking in our mind.

I do not see the basis for the no-profit no-loss approach at all. What the socialistic countries do in this and their pricing policy is in fact quite clear. They do their costing in a different manner. They have the allocations, production programmes and remuneration for what they are able to produce. Their pricing policy has often been criticised—that their consumer prices have no relation to the cost of production. For instance, it is a deliberate policy to subsidise minimum requirements of clothing but clothing, with little fancy. In Soviet Union even scientific books are priced very low; but fancy shoes are priced very high! Within this broad policy framework there is enough room for price discrimination in the public sector. This is a question which I think has not been thought of in India.

We, in the Planning Commission, are still at the elementary stage of a dialogue with the State Governments, merely urging them that their capital investment should pay off. In the Fourth Plan 52 per cent of the State sector investments are on irrigation and power works. If all these works do not yield reasonable returns then what would be the future of the development planning in India ? We cannot just afford to lose on investments.

Similarly, in education, in public health and many other fields we will have to decide what exactly we can afford to do and to what extent. In all these matters, I am afraid, there is somewhat vague and broad generalisation that has gone on for too long in all our planning. It is high time that we delve a little deeper into the problem so that the States are able to harness services and public utilities more systematically for the benefit of state and local finances. With these few observations I have great pleasure in inaugurating this Conference.

PROCEEDINGS

I

Approach to State Taxation

(Chairman : Shri B. Venkatappiah, Member, Planning Commission)

Dr. M. J. K. Thavaraj

As regards the topic on the Approach to State Taxation, it should be borne in mind that this problem was discussed within the terms of reference in the specific context of Kerala. As Dr. Khosla pointed out, the formulation may not be applicable to other States in the manner in which it has been put forward in the context of Kerala. Nevertheless, it brings out certain basic difficulties in the present tax structure and the approaches to taxation which could be considered by other States as well. One of the basic things to which this Committee addressed itself was the relative backwardness of some States and how within the existing financial framework we could bring about a rapid reduction in inequalities in the development of different States. The first two paragraphs of the Working Paper highlight how, during the British period, inequalities had grown and industrial development was concentrated in a few States and cities, making the problem of inter-regional disparity somewhat acute.

Under the existing distribution of financial powers, the States have become increasingly dependent on Central resources and transfers from the relatively richer States to the poorer ones have not been possible to the desired extent. Therefore, it is suggested that there should be some readjustments in Centre-State relations in order to enable the poorer States to catch up with their lags in development.

The paper has also underlined the fact that land and land-based taxes constitute the main source of state revenue apart from commodity taxation. It is found that during the last 18 years, commodity taxes especially those which fall heavily on the poorer sections of the population, have grown disproportionately high. Since one of the important objectives of

Plan development as well as the terms of reference of the Kerala Committee was to bring about more equitable distribution of the burden of taxation, it was felt necessary that one of the basic approaches has to be to move away from commodity taxes which weigh too heavily on the masses of the consumers, to land and land-based taxes.

One of the suggestions that has been made was to switch over from traditional land revenue based on assessment and settlement, to a tax, based on the capital value of the land which would involve a comprehensive machinery for the evaluation of property. Besides, as Prof. Gadgil emphasised this morning, we should pay greater attention to tap all those who have ability to pay in terms of amount of valuable land which people possess and the incomes accruing therefrom in the States. And in order to do that, it has been suggested that an approach may be to move away from the commodity taxes to land taxes based on capital value and agricultural income tax.

The other aspect which has been underlined in the working paper, is that so far, most of the States could not help but undertake the role of a promoter or an underwriter of development. The States vie with one another to lure big industries by offering attractive terms of services. Prof. Gadgil was also drawing our attention to this. He said all these public utility services especially irrigation and power facilities should at least pay their way and they should not continue to incur losses as at present. We also felt that most of the power subsidy given now is enjoyed by sections of industrialists who can easily afford to pay. This has become necessary because of the competition between the States and one State can not afford to lose the possible establishment of a few industries which, with attractive terms, might shift to other States. So the approach is that as far as possible the tariff structure should be so reviewed that at least the public sector undertakings especially the utilities like power, make some decent profit on investments. These are the two basic issues which may be profitably discussed in the Conference.

Shri B. Venkatappiah (Chairman)

Thank you. I should now call upon different members to speak. Within this framework we might discuss

first, the approach to State taxation and then, the problem of resource mobilisation from agriculture. Centre-State financial relations may be taken up later.

Dr. D. T. Lakdawala

Mr. Chairman, the question of approach to state taxation, assumes the basis of Centre-State relations. It is only then possible to concentrate on them.

In order to be sure, that limitations are not very severe, one has to realise, as Prof. Gadgil said, that the powers conferred on the State by the Constitution are not absolutely inadequate. In fact, they are quite substantial in some directions. They are not less than in other federations. For example, in agricultural taxation they are more adequate than elsewhere. Further, the whole realm of property taxation, of consumption taxes, of stamp duties, motor vehicle taxation and the whole sphere of irrigation, electricity and road transport are those which belong to the State, so that the State has considerable power of taxation. Further, these taxes have been fairly elastic, and buoyant during the last 3 years. To an extent this holds good even in certain type of taxes such as land revenue. In the case of other taxes, *e.g.*, sales tax, entertainment duty, etc., even in the past, when these had not been fully exploited, they had been fairly large.

It is true, that some of the central taxes are much more varied and elastic. There are corporation tax, central income tax and so on. But some of the central tax revenues have been less elastic than the state taxes. For instance, customs have been fast falling over the plan period. My contention is that, State's tax powers, in the first instance, are fairly adequate. They are fairly elastic sources of revenue and, therefore, States have no reason to feel unduly constricted by the constitutional provision as regards the tax powers.

The second point I would like to emphasise is that by its very limitation, one talks of state taxation since the State within the Federation has certain limitations even in the exercise of its own taxing powers. It cannot be otherwise. One can again make too much of these limitations. Certain limitations are real. Certain limitations are psychological.

There is very little likelihood that the farmers from one

region will shift away elsewhere, because the tax rates are somewhat different in the States. If one State is richer, its tax policies and expenditure policies are also bound to differ from those of the neighbouring States. We don't have to compare as to what is happening in other States in regard to D.A. rates or taxes. It is not necessary. There are, of course, taxes which in certain States, are being levied at lower rates than in other States. The working paper and the background material have drawn attention to the fact that in order to promote industrialisation certain concessions are being given in electricity rates or sales tax. The only solution to this could be a somewhat regional or all-India agreement on what is and what is not permissible in this respect. But one must recognise that it would amount to a certain degree of uniformity and it is a choice between following more or less the same degree of industrialisation or using one's own powers in the narrow interests of the States concerned.

The idea of state taxation in itself being progressive or regressive is a point on which we might devote attention and it is certainly desirable that if possible, state taxation should be a little less regressive than it is. But when one is talking of taxation, state taxation and local taxation have to be viewed as a whole; when we look at taxation on an all-India basis, national taxes are relatively more progressive; the state taxes are somewhat regressive and local taxes are still more regressive. In a way there are some taxes like tax on land which are regressive. But there are others like the agricultural income tax which are comparatively progressive. To judge state taxation only on its 'progressivity' would be wrong. One must take central and state taxes as a whole for this purpose. One must remember that there are quite severe limitations to the pursuit of progressivity in state and local taxation when they are viewed in isolation. This should be clearly understood. But the most important thing is that if a state wants more services it ought to raise more resources either by raising its tax rates or through improved tax administration and so on. It is not possible that the State can provide more services without resorting to more taxation. There should be a linking between the state taxes and state expenditure, between additional resources mobilisation by the States and between additional Plan expenditure on their part.

Dr. Mathew Kurian (Kerala)

Sir, I would like to speak on two major questions. The first question is of taxes. It is true that during the last three years, may be due to special circumstances, the Central taxes have not been more buoyant. May I request Prof. Lakdawala to clarify whether it is true for a longer period. The second question I would like to raise is about the tax policy and I would suggest that some method should be adopted for evolving a uniform policy of taxation. Prof. Lakdawala suggests that central taxes are sufficiently progressive and States need not worry if their tax system is somewhat regressive. I would like to know the justification for this kind of an argument.

When we are discussing the progressivity and regressivity of state taxation, we are assuming certain levels. Central taxes remain as they are. What is the approach to State taxation ? Why should it ignore progressivity? Why should it confine itself only to resource mobilisation, irrespective of whether the tax structure in the State tends to be progressive or regressive ? The existing tax structure being regressive what is the responsibility of the State Governments? I think the responsibility is to move towards progressive taxation. But there are certain limitations to progressiveness. Some of us had the opportunity to work in the Taxation Enquiry Committee, Government of Kerala, of which Prof. Thavaraj was the Chairman; we started with an enthusiasm for a graduated agricultural income tax. I suggested that in this area, the States could do much. However, there are certain serious limitations. The limitation relates to property relations and the laws of transfer. As it is, agricultural income tax in Kerala is fairly progressive. We attempted to revise it and bring it on a par with the central income tax. Our effort has been to move from the relatively less progressive to a more progressive rate structure. This should be a welcome measure. One should not suggest that the States should not bother about progressivity or regressivity of their tax structure. The efforts of the States should be to bring agricultural income tax to the level of the general income tax. But in doing so, we found that the Constitution which admits that private property is sacrosanct, is allowing for legal transfers of property between the father and the son and so on. Having

done that, if any progressive agricultural income tax is introduced, it would really amount to, as it has happened in the case of land reform legislation, legal evasion. The quantum of resources that could be mopped from this sector is really small. Therefore, property relations and legal rights for transfers constitute severe limitations on resource mobilisation from agriculture.

Mr. Pitambar Pant (Planning Commission)

I agree with Prof. Lakdawala that tax resources, either by having a better tax policy or by imposing new taxes, have not been fully exploited. I would give some figures to show the entire trend from 1951 to 1968 in respect of tax revenues. If you take the total revenue of the Centre and the States in 1950, it was around Rs. 630 crores. That has now gone up to Rs. 3,080 crores, roughly less than six times. In the meanwhile, the revenues of the Centre have gone up from Rs. 430 crores to Rs. 1,900 crores, and if you deduct the land revenue part—it was Rs. 50 crores in 1950 and only Rs. 150 crores in 1968—the residue moves from Rs. 150 crores to Rs. 1,030 crores and it moves as fast as the total of the central revenue.

The second thing is that there are a number of items in the whole list of State taxation, which are being neglected. There is the important provision in the State list of taxation, income from trade, profession and employment. Apart from a few States, no State has cared to look at it. It is stated that there is some constitutional difficulty affecting the exploitability of this source.

The other thing is that even though the Centre has got a large tax base, it transfers substantial resources to the States through certain mechanisms envisaged in the Constitution. For instance, part of the excise earned by the Centre, is transferred to the States through the permissive provisions of the Constitution. To that extent, this is merely a matter of allocating resources from one to the other. But the basic point is that there is an inadequate appreciation of the fact that if India is sovereign and independent and self reliant, its development must be financed by its own people. Irrespective of whether the Centre or the States imposing tax burdens, it is the people who pay for them. In a sense this burden is not real because

adequate services based on the mobilisation are given back to the people. It is in this light that tax powers of the States have to be used to the advantage of the people, *i.e.*, to push the programmes of development. Unfortunately we have lost some ground in this direction during the last few years. In 1965, we were already having something like 14 per cent of the national income as the share of the Government in order to support the developmental and investment schemes. That has now come down. The first requirement is to restore the mobilisation effort to that level reached in 1965. There is no fundamental difficulty. So the first task is to step up the rates of taxes to secure 2 per cent more out of the national income. Of course, I agree that we must have progressive control over resources. For this, we have to identify easier areas and gradually move on to more difficult areas. What is of concern is that no effort is being made in any of these directions which is commensurate with the task we have to undertake. I have in fact closely looked at the Constitution to find out whether there is any serious problem. The Government should place themselves in a position to discharge their responsibilities. I do not see any fundamental difficulty either in the tax base or the progressivity of the taxes: nor should there be any serious difficulty to find alternatives. The lurking hope that somehow or the other the resources will come, whether they come from foreigners or from the Centre is not desirable. If the total tax income comes to 14 per cent of national income, it will not cause any burden of or encroachment on the poorer people and it will maintain an amount of progressivity.

Dr. M.J.K. Thavaraj

I would like to make a brief point. Apart from the question raised by Prof. Lakdawala, and as referred to by Shri Pitambar Pant, there is this concept that at a given rate, due to the growth of the economy, the price situation and other things, there is a growth rate related to different types of taxes. If State mobilisation through sales tax has been significant, it is not all the result of growth at a given rate of taxes. It is the result of continuous exploitation of this source by the State. They have done remarkably well. To my mind, the fact that over a period of time, sales tax has increased by so many times is not by itself a good indicator of its buoyancy or elasticity. Secondly, the Central

Excise does also pay considerable amount of rebates. These rebates are not there in any significant measure in the sales taxes. So whatever enhancements in the rates have taken place, they grow without any net reduction in the tax arising out of rebates given to the tax payers. There have of course been few exemptions here and there but they have been marginal.

I agree with Shri Pitambar Pant when he says that we are engaged in an effort of mobilisation to match a bigger Plan; but, as he himself cautioned, we ought to, at the same time, know that any mobilisation will automatically bring about commensurate benefits to the sections which bear the brunt of the burden of taxation. Any State which is progressively inclined will always be bothered with this problem. We ought to bear this in mind.

Shri K. S. Narang (Punjab)

I do feel, with my experience as Finance Secretary in the Punjab, that there is a vast field which remains unexploited. Over a period of time the Finance Commission and the Planning Commission, have so functioned that the States received little incentive in exploitation of whatever resources were available to them. In fact this is one point which all the States have been urging before the Finance Commissions. If there had been some incentives available to the States, then the States would have been definitely prompted and encouraged to exploit whatever resources are available to them. I grant that State resources are not as elastic as those of the Centre. I also grant that the States are entitled to get grants-in-aid from the Centre under the Constitution. There is also the question of devolution and the extent to which devolution should take place and the allocations as between State and State. If the Centre had been vigilant enough we would not have run into these difficulties. I must say that these are my personal views and must not be taken as the views of my Government.

I may also say that taxation is not the only source of raising revenues by the State Governments. There is also a vast field of non-tax sources and in fact the Kerala Committee has gone into the details of non-tax mobilisation. In Punjab I find that non-tax sources yield as much resources as

taxes. For instance, we receive income from the State Farms. These should correspondingly go up with the investment. Well, whether it is leakage or something else, the fact remains that the extra incomes that shall accrue have not accrued to the State. In a sense, over a period of time we have been subsidising them. With incentives and sound financial management, we should have had better results and the States would not have been as badly off as they find themselves today. There is the question of public utility; there is the whole question of irrigation system and of power. If appropriate steps had been taken in time the whole approach would have been one of resource generation and not merely satisfied political aspirations.

If we really want this financial problem to be tackled, it cannot be done in the spirit in which it is being talked about all along in the newspapers. The Centre must tell what the States can mobilise and what their exact requirements are. The Centre must give more funds by way of devolution to the States, but this should be only after an assessment of the situation as to what the States can really do in this regard and what their actual requirements are. Taxation is in a very important sense a political process. There cannot be any doubt about this. It is in fact this limitation which has been standing in the way of our mobilising resources. I feel that in almost all the States there are resources available but they have not been tapped or taxed and our limitation is political. We have also to shift emphasis from commodity taxation to tax on land, wealth and income. I do not know of any country where the commodity taxation can or has been given up altogether. We have to necessarily go for commodity taxation but at the same time there has to be a happy balance. The Planning Commission and economists all over the country have clearly stated that more incomes are generated in the rural sector. The reason is obvious. Whatever discussion we have here would not be of any great significance unless we can take steps to bring in the politicians into the whole range of these discussions.

Shri R. N. Malhotra (Madhya Pradesh)

I find that the discussion has strayed into more general aspects of the matter. I think enough has been said on the

question as to whether under the Constitution, the States have certain rights of taxation which have potentials of growth and how we fare in tapping the tax potential. I am in agreement with the view that perhaps not enough can be done to tap the resources available in the field of taxation allotted to the States. On the other hand, tax powers given to the Government of India under the Constitution have been politically easier to operate by virtue of their very nature. There is broad agreement that there ought to be progressivity in taxation—whether in the personal field or corporate field. It has been possible greatly because of its very nature, to gather excise taxes at certain limited points and that is why perhaps we find that proceeds of Central taxes have gone up over a period of time. As for commodity taxation—as very rightly pointed out, it has been tapped to a considerable extent. States, of course, have been concentrating on sales tax, since it was easier despite its regressive aspects. All the States, especially those which are backward and trying to develop, have been compelled to resort to commodity taxation which is regressive in character. I know of some countries which are much more backward than India and where commodity tax is not so important. But some of the Governments in African countries have been compelled to levy certain tolls and taxes on families and so on irrespective of the relative incidence on different classes of people. I personally think that this country is at a certain stage of development where it must call upon all people, rich or poor, to contribute their mite. I am not against progressivity; it has to be there; but, by mere progressive taxation a country like India cannot achieve the desired results. I wish that aspect of the matter is borne in mind. It is being done in various forms, in various types of economy. I have still to come across a country which has gone ahead without some type of taxation whether it is contribution in the shape of cash money or in the shape of labour fully compensated by adequate wages.

The main problem is how far it is possible to shift to a progressive group of taxes. There is no doubt that this package of taxes has not so far been properly tapped. There are certain practical difficulties inherent in these taxes. One of the difficulties as pointed out by the Finance Secretary of the Punjab is, of course, political which is inherent in say, a tax like land

revenue. I remember that in 1967-68 we had been able to push through up to the budget speech level, a proposal which was to the effect that all land and all houses would be taxed at a certain rate on the basis of their capital value. Now when this matter went to the Legislature the legislative party in power did not allow it to go through. It is interesting to note that the criticism came not from the vested interests: but from the legislators who restricted the move on the plea that such a tax would be inconvenient to the people at large and especially to the small peasantry.

So far as land revenue is concerned assessment does not pose any difficulties whatsoever to the tenant or to the cultivator. But a tax based on capital value would involve periodic assessments—annual or quinquennial—and would not be palatable to the peasantry.

Another sphere in which I have personal experience is sales tax. I know how inconvenient it is to administer sales tax. I dealt with sales tax appeal case, where the total amount involved was Rs. 150. I knew, however, from personal knowledge that the person who had come to me in appeal had already spent Rs. 400. This is the kind of problem we run into in sales tax administration.

In Madhya Pradesh, in 1967-68 holdings measuring 7½ acres and below were exempted from land revenue. This exemption limit was later raised to 10 acres. We pointed out that the grant of concession to small holders might be theoretically justifiable but there were many considerations which weighed against such a step. Firstly, the incidence of tax on the small holder is really insignificant. We advised the Government that ban should be placed on partitions so that holdings did not become uneconomic. But the Government was unwilling to place any such restriction. They were confident that there would be no further sub-divisions. But the moment this exemption was given income on registration stamps went up, on account of subdivision of land holdings to avoid tax liability. We had the same fate with regard to ceilings legislation.

I am in favour of introducing an element of progressivity in land taxation; but, as it stands today, I wonder whether it would be possible for us to change over to a taxation based

on capital value with a view to ensuring progressivity. I have my doubts.

The same type of difficulties might arise even in the case of agricultural income tax. I do not think it would be possible for any political party today to say that the limit of exemption for agricultural income tax should be lower than that allowed in respect of other incomes. We are all aware how ceilings legislation has been completely defeated. Against this background, I wonder whether agricultural income tax as a new impost would be successful. I personally think that a system of income taxation which makes no distinction between income derived from agriculture and income derived from other sources would be more successful than one exclusively designed to tap agricultural incomes. Taxing agricultural and non-agricultural incomes separately would result in loss of revenue to the Centre as well as the States. Combined income tax would be the most effective way of dealing with the new rich in the rural sector.

The rates of land revenue could be enhanced and there should be no provision for any exemptions. This is the only way to raise resources in a backward country with many small cultivators. If this is to be done, the present trend in many States will have to be reversed. Prof. Gadgil remarked this morning that probably land revenue cannot be reformed. I disagree with his proposition. It must be reformed if any type of meaningful tax is to be introduced in the rural sector.

Another suggestion is that it might be very useful if the Government of India or the Planning Commission or some State Governments were to undertake studies about the economics of various kinds of power-using industries which have come up in recent years, for instance, the caustic soda, aluminium industries, etc. Let us find out the level of tariff which is reasonable in order to assure fair return to the industry. Today such studies are not made. The private sector will always say that their unit is not going to be economic unless the rate of electricity tariff is sufficiently low. This is true even of public sector undertakings. For instance, for some years, the Government of India has been pressing that unless the M.P. Government gives substantial concessions the proposed aluminium plant will not be economic. It is imperative that the economics of these units are gone

through carefully. Otherwise, the State Governments will be burdened with a lot of subsidised services which would continue to be a drain on their limited resources.

Shri J. Shiva Kumar (Tamil Nadu)

We have some practical difficulties. My submission is that the size of the State Plans should be related to the tax burdens borne by the State Governments. There are certain commitments borne by the States, such as the dearness allowances arising out of the fiscal policies pursued by the Centre. Therefore, such commitments ought to be adequately met by devolution of taxes.

Regarding the suggestions of Prof. Lakdawala on the character of state taxation, I do not see how the State Government could be altogether unconcerned about the regressiveness of state taxation. The nature of state and local taxes are basically regressive; but the State Governments are helpless in this regard. As for the rates charged for public utilities and other services such as electricity tariffs, I may say that these are conditioned by the severe competition from the neighbouring states and it would be very good if the States could get together and adopt a uniform tariff policy.

Shri G. V. K. Rao (Mysore)

A question has been raised regarding the role of the States in preventing shifting of resources from relatively poor States. One of the points made by Prof. Gadgil in his inaugural remarks was about irrigation and other projects. A lot of money has been invested on irrigation projects in the last three plans and a much higher amount will be invested in future plans. It is true that the states are losing a lot on irrigation projects showing thereby that there is something wrong in our manner of financing irrigation projects. We should change the system of financing irrigation projects in such a way that the entire money for irrigation projects is met out of irrigation rates and betterment levies. But because of organised opposition these levies are difficult to collect. This state of affairs cannot be allowed to continue. I suggest that we should change our system of financing irrigation projects on the lines pursued by the Bureau of Reclamation in the United States. There they break the cost of the project in terms of its various components such as flood control,

irrigation, power, industrial and municipal use, recreation, fisheries and so on. The cost of flood control is borne by the Government. But, the cost of irrigation, municipal water supply and so on are recovered in full from the persons who benefit by them. These costs ought to be recovered with interest which may be somewhat lower than the market rate. Similarly, industrial use of power and water should be fully charged on commercial basis. Water rates may vary from project to project depending on the relative costs of projects. The practice of charging the same water rates or betterment levy should be given up. My point is that public utility services should, as far as possible, be self-financing. All the States are very keen to increase the area under irrigation. This would involve a large volume of investment, which would be difficult unless it pays its way. Projects should not be undertaken because of political considerations which often disregard the economics of the project. Electricity tariff has been a real problem for many of the states because it is difficult to attract some of the power-intensive industries without giving them substantial subsidies, especially in the face of inter-state competition to attract such industries. Any loss of revenue on this count tends to throw a heavy burden on the general revenues of the States. The same is true of rural electrification.

Such limitations are also operating where diversion of trade is an important consideration which State Governments cannot afford to ignore.

Shri Mani Narayanswamy (Mysore)

I would like to seek some clarification on the sentence on page 68 of the working paper. "Only a carefully worked out programme of land nationalisation coupled with suitable measures of taxation appears to be the real answer to the problems created by speculative dealings and unplanned use of urban land." What does land nationalisation really contemplate?

The second point is about agricultural income tax. I think we need to put some figures on our somewhat optimistic ideas about agricultural income tax. Most States are levying agricultural income tax. We are doing it on plantation industries. This area of agricultural activity yields us quite a lot of revenue

but we are not sure whether by extending the tax in its present form we would be able to mop up a great deal of wealth that is accruing in the rural areas. It is said that in the rural areas some people are making a lot of money. But on the whole, if you take an absolute figure, we will not get adequate resources through this tax. If that is so, I would question whether it can be looked upon as a potential source. It is no use being doctrinnaire in this matter.

A lot has been said about competition in the field of sales tax among States. Regional approach to sales tax is already there. As one of the speakers remarked, what is required is a national policy on sales tax. We have now begun to delimit the items and put certain limits to tax rates. This procedure may fruitfully be improved. In my view, the impact of sales tax concessions is somewhat exaggerated. As Finance Secretary, I have to resist some demands on exemptions of sales tax to industrialists purely on the ground that some other States are giving these concessions and incentives. It is true that such concessions have an effect on the revenue resources of the State. But we are under pressure and I think we should try to arrive at a general principle which ought to govern such incentives. This is a matter which we have referred to a committee, which we have recently set up. But I think it is a matter which requires some general consideration as well.

Dr. M. J. K. Thavaraj

I would like to give just a brief explanation as to what is contemplated by the term "land nationalisation". It is not nationalisation, *i.e.*, taking away private land. It envisages that the development authority or some such agency could through a self-financing mechanism, earmark land and see that the land use in the urban area is made in an orderly manner as referred to by Prof. Gadgil.

Shri B. C. Ganguli (West Bengal)

From the trend of discussions, I find that most of the participants seem to believe that land is a source of revenue which could be more intensively tapped than now. May I put it that most of the States have placed ceilings on lands. Consequently, the possibility of mobilising large amounts from land is remote.

Why don't we face this fact ? We are discussing a proposal here. We are not going to lay down policies and procedures. Land has only limited tax potential. Land revenue is gradually being given up in most of the States. It is not going to be revived. My point is that the commodity-base idea of taxation should not be so repellent. There is another suggestion to levy land revenue based on capital value. Ascertaining the capital value involves a complicated and expensive procedure. The machinery for capital valuation may become so costly that the process may become difficult. My idea for your consideration is that as the income tax is administered by the Centre and a part of it goes back to the States, I wonder why the present income tax laws and the wealth tax laws cannot be extended to agriculture.

Shri J. L. Kundu (West Bengal)

I think Prof. Thavaraj has done a useful thing in drawing our attention to the possibility of imposing property taxes. But in this matter most of what I would have said has been said very clearly by Shri Malhotra from Madhya Pradesh. I would add that though taxation on the basis of capital value on agricultural land is going to be difficult, there are better prospects in this sphere so far as urban land is concerned. This aspect should be looked into more urgently. If an assurance is held out that the proceeds would be largely utilised locally, on local improvements in the urban areas, it may not encounter very great opposition. At the same time, by its very nature, a tax based on this kind of valuation is going to be more costly to collect than a tax like the sales tax. There has to be an evaluation and naturally the assessee has to be given some opportunity to appear before the court and so on. In the case of sales tax, our experience is that the cost of collection is of the order of 1 per cent but in the case of land revenue, it is much higher and in the case of property tax based on valuation it is going to be much higher.

As regards income tax, I agree that it does not hold out much scope. We have such a tax both on plantation industries as well as other agricultural incomes. The proceeds from the other agricultural incomes are somewhat negligible. They may possibly improve to some extent if the collection agency is the same as the income tax agency so that the possibility of evasion

is minimised. But nevertheless in a State like West Bengal the possibilities of agricultural income tax are almost negligible. In the Punjab, it could be different.

As regards motor vehicles tax and octroi, we are in a difficulty. If we increase it in response to the suggestion of the Ministry of Finance, the Ministry of Transport will come round and say that already road transport was taxed heavily. The Transport Ministry is still considering the recommendations of the Keskar Committee but, in the meantime, it has practically asked us not to do anything in the matter.

While certainly we should look more in the sphere of property taxes in future, I feel the taxes mentioned in Article 269 of the Constitution have not been fully utilised or investigated by us. On the other hand, a tax on passenger fare has been abolished and whatever we are getting now is not sufficient compensation for that abolition.

There are several other taxes mentioned in that Article which have not been properly utilised and our correspondence with the Finance Ministry in the matter has not carried us very far.

So far as public utilities and irrigation works are concerned, I fully agree that they must pay their way. If we have to go in for public utility works, I do not think it will be financially possible for us to carry on unless they pay their way. I think the mistake which some of us have committed is that when a particular irrigation work is ready, we start giving water free and then later we impose a small rate only to find that we cannot increase it further. That mistake should be avoided in the future. We should try to fix a rate from the beginning which is reasonable and practicable. It is our experience that even the current maintenance cost is not recoverable on account of the low rates fixed.

Shri Pitambar Pant

Will not the extension of income tax and wealth tax to agricultural incomes present constitutional difficulties ?

Shri B. C. Ganguli

I think on the capital side of it, the Centre has powers.

Shri N. G. Abhyankar (Maharashtra)

That development on a large scale is not possible without paying for it is now widely being accepted at the state level. If we have to finance our plans, we have ultimately to tap the agricultural sector. We have ploughed in quite a bit of resources in the agricultural sector in the course of the last 17 years of our planning. But our mobilisation from this sector has not been commensurate. So far as the agricultural income tax is concerned, it may be possible to reduce the minimum limit that is prevalent in Maharashtra. But we have to recognise that Maharashtra is a State where majority of the holdings is below five acres. About 25 per cent of the area is affected at least once in three years due to widespread failure of monsoon. Consequently the scope for mobilisation through agricultural income tax is limited. However, in the transitional stage it should be possible to mobilise through measures like education cess, which will ultimately produce substantial revenues to the States. We are not unmindful of it especially in view of the fiscal measures which Andhra Pradesh, Mysore and so on have adopted, in recent years. On the other hand, there are difficulties in tapping resources through agricultural income tax, or water rates or through economic tariffs in the case of rural electrification and other public utilities. For instance, in the case of rural electrification, the farmers are to be encouraged to use power for pump sets through subsidised rates for two or three years.

We have given consideration to questions like increments in land values in urban centres like Greater Bombay. Such capital gains ought to be tapped.

Shri M. L. Batra (Haryana)

I am of the opinion that state taxes are not as elastic as they ought to be, nor, such as they are, have they been fully exploited. There is considerable scope for additional revenue to be raised from them. Much of the additional land revenue which can be gathered is out of proportion to the increases in productivity as well as agricultural prices. There are, of course, political reasons and practical difficulties in raising the rate of land revenue. We have been thinking on a number of other proposals by which we could get results. We have a proposal to impose a development cess on land and relate it to development works, rural

electrification, education and so on. We hope that we should be able to earmark some additional funds for this sector. It is well known that water rates are unremunerative. We are incurring considerable deficit on this account.

It is maintained that one need not worry about neighbouring states having different policies and rates about land revenue, water rates, dearness allowances and pay scales of government employees, and so on. It is very difficult to accept the proposition. It is well known that all over the country dearness allowance has been brought on par at Central Government rates. We are also at considerable pressure to bring our pay scales as well as D.A. on par with the Punjab. Similarly, it is extremely difficult to persuade the legislature or the electorate that higher rates of taxes than the neighbours are necessary and justified.

I would like to refer to the cut-throat competition among States with regard to the pricing policies of their public undertakings and industries. States are subjected to enormous pressure to give subsidies and tax incentives to industries. Different States vie with one another, in attracting industries to their States. I think something should be done about it. The only body, which can help in this matter, is the Planning Commission. I think we should lay down certain ranges within which the States should formulate their pricing policies. I am afraid that the prevailing inter-state competition will dry up this resource potential of the States.

Dr. S. R. Sen (Irrigation Commission)

In my view, the discussion about the progressive and intensive character of taxation has been carried too far. I think it is wrong to consider any one tax in isolation. Tax system as a whole comprising of the central and the state taxes should be considered to determine whether it is progressive or regressive.

The second point is about elasticity. As has been mentioned by various speakers there is considerable elasticity so far as state taxes are concerned. Why is it, it has not been possible to exploit it fully ? The reason is as you know that the politicians who have to take decisions about taxes are living in a highly competitive world. Such competition is real. And therefore we have

to devise means and methods by which politicians' task is made easier. I suggest that the next Finance Commission consider some ways of providing incentives to those who show themselves responsible enough to raise resources as against those who are reluctant to do so.

We, sometimes, give up old things before we make sure of the new things. There is a common saying that an old tax is no tax. People do not feel so much about the burden of old taxes. We should not give up the old tax unless you are sure about a new tax. Recently I had a discussion in a State. They gave up land revenue of half a crore of rupees. They said that they will make it up with agricultural income tax. But they collected only Rs. 7 lakhs through this new device. It has had a very adverse effect on the resources of the State.

Chairman : Where was this ?

Dr. S. R. Sen

Orissa. I think it is important for us to emphasise that any old tax should not be done away with, unless we have made sure that the new tax will more than compensate it.

The other thing is that we should make a distinction between taxes (where there is no *quid pro quo* relationship) and other levies such as those on agricultural imputs. We are providing electricity and other inputs for agriculture which augment the income of the farmers. Thus there is a direct relationship between services provided and productivity of agriculture. The Government would be justified in netting a portion of this increased income through suitable taxes on land and the income arising therefrom.

The prevailing mood in the country is to secure as many free and subsidised services as possible and not to pay any taxes. There should be some way of breaking this resistance to tax. If there has to be a change in the Constitution that should be done. If we impose income tax on agricultural income, counting agriculture and other property together, whatever money is collected should be given to the States and should be spent on what is popular in the States. I would like to hear Dr. Parmar who is the only politician present here, about collecting income tax or wealth tax and then handing over the money to the States.

Dr. Y. S. Parmar (Himachal Pradesh)

My own view is that it has been rightly pointed out from the beginning that the whole policy about taxation and utilisation of funds has been miscarried. We are bemoaning rather late in the day because the facilities and the concessions we have given to the people, whether it is the Central Government or the State Government without a return are something difficult to retrace. But we have to do so. My view is that if I get certain benefit I must pay for it. The harm done is that the benefits never reach the poor man. There is no getting away from the fact that States have to face up to this problem much more seriously. In the case of agricultural income tax the peasants will not mind sharing their prosperity but they are afraid of the harassment of inspectorate staff. Anyway it is a matter to be considered.

But I am in agreement with the proposition that the States ought to raise their own resources. Public expenditure on irrigation has conferred large benefits to the farmers. We should be able to get back something in return by way of increased taxes. There is need for a machinery to look to the spending of money. Otherwise there is going to be serious trouble.

II.
Centre-State Financial Relations

(Chairman : Dr. Y. S. Parmar, Chief Minister, Himachal Pradesh)

Dr. Y. S. Parmar

It would be better if we confine ourselves to the points for discussion raised on page 71 of the working paper.

Shri G. C. Pukhan (Assam)

I am fully conscious of the great burden placed on the Centre. The Centre should have certain sources of revenues which not only have buoyancy but have the character of being exploitable at short notice during national emergencies. Income tax is one such device. It may also be good to combine both agricultural and non-agricultural incomes for purposes of taxation. If need be, I am in favour of amending the constitutional provisions governing such tax powers. This is one of the important matters that we cannot forget while discussing Centre-State financial relations. Under the present law, capital gains in respect of agricultural land is not liable to taxation. The law should be suitably amended. There is certainly scope for raising more revenues from the agricultural sector. But there are certain limitations. In India unfortunately as there are regions affected by drought and floods; agricultural tax will fluctuate from year to year. We have also to remember that rural debentures will also affect the small savings campaign.

I have one more suggestion. There is a tendency to make the bridges toll-free. A device may be adopted by which an over-cross bridges-toll may be charged. I do not see objection in the amalgamation of the taxes with railway fares. Again, the system of additional excise duty in lieu of sales tax on certain commodities is coming in for lot of criticism. I am of the view that the scope of variation of these excises is not as much as in

the case of sales tax. I think now the Central Government may bring in necessary legislation in the system by providing for *ad valorem* excise duty instead of specific duty and also increasing their additional excise duty.

I do not agree that the Concurrent List is a focal point for gravitation of powers towards the Centre. Of course, I have some reservations on policies followed by the Union Government which we consider undesirable. In certain commodities Union excise tends to narrow down the scope of sales tax. For instance, while the state of Assam would like to impose a tax on tea, the Union Government says that being an export industry, such a tax should not be imposed.

Gujarat and we hold common brief on the rate of royalty on crude oil. These are not matters affecting the Constitution but only the procedure followed by the Central Government.

I do not see much scope in trying to bring in large scale constitutional amendments on financial matters. I would say, that particularly in the case of backward states, they are not going to get any benefit by amending the Constitution.

So far as the debts are concerned, the unfortunate thing is that the patterns of financial assistance evolved during the three five year plans and the three annual plans have laid a large burden of debt on the states arising out of their pursuit of unremunerative schemes. In their anxiety for development the States have taken a lot of loans without thinking of their consequences. As a result large amounts have been borrowed for purely revenue expenditure. So there is strong case either to write off those loans or convert them into long term loans repayable at nominal rates of interest.

For instance, projects of administrative buildings and college buildings costing a lakh or more are considered as capital assets and for those purposes loan assistance has been admissible. It is a well known fact that administrative buildings or college buildings do not bring in any return. As such there is need for a thorough study in regard to loans taken by the State Governments and for servicing them and bringing them on such terms of repayments as will relieve the States of hardships. At present, the financial difficulties of almost all the States are due to the

heavy debt burden. This, however, is only an aspect of the Centre-State financial relations which needs looking into.

Shri M. L. Batra

I think too much has been made of the States' resources of taxation being inelastic and of the Centre's being elastic. It is also being said that the responsibilities cast on the States are quite numerous and the resources available cannot cope up with them. There is a point in that. But I am of the opinion that the Centre has its own responsibilities, and the constitution-makers in their wisdom gave our country a strong Centre. Ours is not a federal form of government. It is somewhat federal. It is somewhat federal in normal times but it can assume a unitary character during times of emergency. Under the Indian conditions, it would be a mistake to weaken the Centre. I am, therefore, not in favour of our amending the Constitution so as to transfer some sources of revenue from the Centre to the States. Within the framework of the present Constitution, something can be done so that the States have more powers to discharge their responsibilities. It is in this context, that the role of the Finance Commission becomes very important and I think much can be done to redress the grievances of the States through the agency of the Finance Commission. One of the members of the Finance Commission is here but I may be permitted to say that grants-in-aid given under Art. 275 as a result of the recommendations of the Finance Commission has led to a sense of irresponsibility and lack of prudent financial management because, when the State Governments know that any gap on their revenue account, would be filled by the Centre, they are not particular to take remedial steps themselves. Art. 275 allows grants-in-aid of revenue. How is that grant determined? It is determined on the basis of the deficit on the revenue account ? If a state manages its affairs prudently it gets less amount of money on account of grants-in-aid.

So, the Finance Commission should fix norms for expenditure as well as for raising revenues.

The other point is about distribution of Union excise duty. The Centre, on the recommendations of the Finance Commission, has been giving a share of the excise duty to the States. But

considering the resource position of the States, the Centre should allow a greater share to the States from the Union excise duties. I would go to the extent of saying that it may be 50 per cent of the proceeds of the Union excise duties.

Similarly, in respect of income tax, a greater share can be allocated to the States from the proceeds. Today, it is 80 per cent. It can be even 90 per cent. My point is that within the fiscal framework envisaged in the Constitution, it should be possible for the Centre to transfer larger resources to the States.

A question has been raised with regard to additional excise duties on certain items. I shall stand corrected. My impression is that all the States have represented that this power should be transferred back to them as they have suffered adverse consequences of revenues. That, I think, should improve the finances of the State Governments.

Whether there should be a Special Finance Enquiry Commission for straightening out some of the problems should be explored. I am, however, against the demand that there should be an amendment of the Constitution to allow more powers of taxation to the States.

I have already referred to the question of re-scheduling of debts. It is asked as to how the fiscal arrangements between the Centre and the States should be altered to augment the free resources of the State; to scale down the indebtedness to manageable proportions; and to transfer adequate resources to the poorer states so that they may have enough elbow-room to adjust their developmental plans. I entirely support that there should be rescheduling of debts. As a result of multipurpose projects which were heavily capital intensive, some of the States are finding it very difficult to repay the loans. It practically leaves them with little money for other areas of development.

The other point is that enough should be distributed among States. I would like to say that this sort of *ad hoc* assistance would not be the right thing to do. The NDC resolution has allowed assistance to backward States on certain basis. But backward states have special problems. This NDC formula cannot take care of backward states adequately.

Shri B. C. Ganguli

A question is raised as to whether it is desirable to constitute a high-powered commission to review the various constitutional issues and practices affecting Centre-State relations or whether as recommended by the ARC Study Team Report on Centre-State Relations, a Special Finance Enquiry Commission could be constituted to examine the question of widening the base of devolutions and of prescribing the share of divisible taxes in the Constitution itself. Besides, the working paper poses the question whether it is desirable to bring the Centre's role in the concurrent and state subjects within the purview of such a Commission.

I am in favour of the suggestion that there should be a special Finance Commission which should go into the whole question of devolution from the Centre to the States. It can also consider the question of bringing the Centre's role in concurrent and state subjects within the purview of the Commission. I would certainly say that loans and grants should be given by the Centre for productive schemes and outstanding debt should be written off. I do not think any general view can be taken here. Individual cases may have to be considered. That is a different matter. As for the question whether it is possible to allow the postal and small savings receipts to be used for productive schemes, I would like to make the following observations. At present 2/3rd is being allotted. We may recommend that it may be raised to 3/4th—whether we can go beyond that or not, that has to be considered.

L.I.C. could be persuaded to be more liberal to the State Governments in lending them necessary resources.

I am not quite convinced about the wisdom or the efficacy of a permanent Finance Commission with a permanent Secretariat for improving Centre-State financial relations. We have been saying that there should be one body both in respect of allocation of Plan and non-Plan finances on capital and revenue account. I do not know whether it is necessary to have a permanent Finance Commission. The NDC could perhaps consider this matter. NDC certainly have a great say in all these matters and it would be best to leave this matter to it.

In what ways could the NDC be strengthened and developed for high level decision-making on all issues of national importance in planning and policy-making for development is a question which, in my opinion can best be left to the NDC. I am not quite sure what is exactly implied by it. The present body, as it is, consists of all the Chief Ministers of all the States and the Planning Commission provides secretariat to it. I think that arrangement is satisfactory.

Shri J. L. Kundu

The first point I would like to comment on is regarding ways in which the fiscal arrangements between the Centre and the States might be altered to augment the free resources of the States enabling them to scale down their indebtedness to manageable proportions; and to transfer adequate resources to the poorer States, etc. I should say that the present system of devolution as also plan grants made through the Planning Commission requires some rethinking as to whether we could in some way or the other, establish some relationship between the tax effort which the State has to make and the assistance which it should get. I do not mean to say that the entire assistance should come from the Centre but at least part of the assistance should have some relationship to the taxable surplus.

About debt rescheduling, we have already talked sufficiently. I think it is necessary and it should be done. I believe it is being worked out now. All I can say is that unless this is done our finances cannot be set right.

As for helping the poorer States, I have not quite understood what is implied. In the present system of devolution and Plan grants, this is already done to some extent. I do not know whether any further improvement is required in this sphere.

About constituting a high-powered Commission to review the various constitutional issues and practices affecting Centre-State relations, I am not sure whether we should go in for it so soon after ARC report. It is not desirable to go on multiplying the committees and commissions.

About the point whether it is possible to allow the entire amount of the postal and small savings collection from a State to be used in the State for productive schemes, I am at one with

my previous speaker that the entire amount cannot be handed over. After all it is being handled by the Government organisation, namely, the Post Office and the Small Savings Organisation. So I would only support what has already been stated earlier that about 3/4th of the savings collection should be handed over. If we could push the proportion a little higher, the possibility is that Government would lose interest in the effort. At present 2/3rd is being handed over as loan. This is the net collection which the States are adding from year to year. There should not be any question of repayment of the net collections which we borrow. We pay interest but there is no question of repayment. Well we have been urging this on the Government of India for some time but they have till now avoided any reply.

On the question whether the LIC could be persuaded to be more liberal in their lending policies to the State Governments and their undertakings, I certainly agree that they can and should do it. But so far their response has not been very good.

Regarding the question whether a permanent Finance Commission could improve Centre-State relations, I am inclined to think that there is some need for it. I do not mean to say that the Commission would be always in session or always at work, but then the period of five years is too long and as we have found out during the last few years, the financial picture of a State has been changing so rapidly that it is too long a period. For instance, after the award of the fourth Finance Commission, my State, and I believe, all other States also, have been compelled to incur a considerable expenditure which is not covered by the award of the fourth Finance Commission. They have not been doing so for any pleasure but through sheer force of circumstances. They have not done so in the expectation that the fifth Finance Commission will come and make up for all this expenditure. The expenditure has already been incurred and the fifth Finance Commission is not going to recoup us for what has been incurred in the earlier years. I do not think States have incurred expenditure merely guided by the fact that future Finance Commissions would provide for such expenditure. As a matter of fact we did not know that the fifth Finance Commission was coming when we incurred such expenditure. We had gone on increasing dearness allowance

which to some extent could not be resisted. I would like again to emphasise that States have not been encouraged in any way by the present system of devolution which should be modified to operate in such a manner that they are encouraged to go in for further taxation.

About strengthening the NDC I am of the view that at this stage nothing much can be done about this. NDC being what it is—a body outside the Constitution and outside the law, will always remain an advisory body. But the scope of its advice might be widened. It may have greater say in all such matters. It may render advice only on major economic issues not only affecting just Centre-State relations in financial matters, but all national matters of importance.

It is not clear to me in what ways it is possible to evolve a code of ethics governing the Centre-State financial behaviour.

Shri N. D. Tiwari (Uttar Pradesh)

Most of the previous speakers have admitted that the States have not fully exploited the sources of taxation which are already available to them. Under the circumstances a case would have to be made out for transfer of certain sources of taxation from the Centre to the States.

In the very nature of things certain tax powers like customs, income tax, etc., will have to be vested with the Centre. If customs is given to the States, it would benefit only those where major ports are located. Similarly, if the power to impose income tax is given to the States then only those States where head offices of certain companies happen to be situated, would benefit by the tax. So I do not think it is possible under the present circumstances to transfer any sources of taxation from the Centre to the States though there is a case that the revenue that is collected in the pool at the Centre, could be transferred to the States in accordance with certain principles; and the constitutional machinery is always there in the form of Finance Commission. As for the new element and the new dimensions of responsibility which the States have assumed under the plans, the Planning Commission has largely taken care of this. So as far as non-Plan finance is concerned, there is the constitutional machinery of the Finance Commission and as far as plan expenditure is

concerned some criteria have been recently developed by the NDC for transfer of resources from the Centre to the States. No State is satisfied about the quantum of assistance from Plan or non-Plan side. Such a widespread dissatisfaction by itself would not justify any change in the constitutional framework.

Most of the speakers have agreed that in the circumstances we are placed, we need to have a strong Centre. Maybe at the back of this question which has been posed, is the suggestion that more resources should be transferred from the Centre to the weaker States. How can such transfer of funds take place unless the Centre has the command over finances ? The planning process has unfortunately generated irresponsible behaviour in the matter of expenditure. I think nothing was wrong initially with the distribution of loan and grant component of financing a particular scheme. Even the so-called productive schemes have not generated resources for the repayment of loan. For instance, irrigation and power schemes, which are productive schemes, have not generated resources. So if the investment has not been done wisely, if there has been a certain amount of irresponsibility in expenditure, if certain well accepted canons of expenditure have not been followed, we cannot say that the loans should be written off. It will only lead to further irresponsibility in the use of funds. In fact we should remember that credit is a good servant but a bad master. We give this piece of advice to the cultivator but we forget it at the higher levels. If credit is a good servant, if used productively, it should not be difficult to repay the loan.

In fact it has already been agreed about repayment schedule. I am not in favour of writing off loans as it will set a very bad precedent for the future. Someone has suggested that the present formula of distribution of Central assistance takes care of the needs of backward states, to the extent of 10 per cent of the allocation of Central assistance. It means Rs. 350 crores for the Fourth Plan period and Rs. 70 crores per annum. When distributed between a dozen or so of backward states the amount so made available would hardly scratch the surface of backwardness. It would be no more than a relief of 2 or 3 rupees per head of population of the backward states per annum.

The other suggestion is that a sort of permanent machinery

should be created to deal with inter-state financial problems. Will it be desirable to have a situation of flux all the time ? When lobbying and pressure will be exercised every minute and every month ? After all a sort of finality about the availability of finance between the Centre and the States is something also to commend itself. Personally I feel that this matter should be settled for a period of time, so that the exigencies of political situation are not allowed to come into the planning process. I have already submitted that no case should be made out for writing off the loans utilised for unremunerative purposes. If irrigation and power is unremunerative I cannot recall any other thing which is called remunerative as far as state sector is concerned. When patterns of assistance were determined adequate care was not shown to ensure that only productive part of plan outlay would be covered by loans. Incidentally the manner in which the plan finance has been used has also affected the repaying capacity of the States. Well the political atmosphere in the States has been responsible for some misdirection of funds. If in this process, the common man has not adequately benefited, how can we expect him to accept increasing burden of taxation ?

As far as institutional finance is concerned, it does not need any argument that these institutional finances will be increasingly available in backward states. According to one of the papers circulated by the Planning Commission, 52 per cent of the institutional finance has been invested in six metropolitan cities. It is for the NDC to take purposive decisions on the economic issues. As of now it is not much more than a debating society. I would not, therefore, place much hope on the NDC in the prevailing political atmosphere.

Shri M. L. Batra

One of the conclusions arrived at in the papers circulated to us, is that dependence of the States on the Centre has increased both in respect to expenditure on Plan as well as non-Plan revenue and capital. The other conclusion which has been arrived at in these papers is that the Centre has got enormous command over relatively larger and larger revenues. The third is that such a command over resources has not brought about the requisite transfer of resources to reduce inter-regional

disparities. These points have been supported by necessary data which have been circulated. It is in this context that the question of Centre-State financial relations has been posed.

My feeling is that in view of the enormous tax base conferred by the Constitution on the Centre, it is desirable to have a fresh look at the Centre-State financial relations with a view to reducing the increasing dependence of the States on the Centre.

Such dependence has resulted in certain unhealthy trends. Dependence psychology weakens initiative and prudence on the part of the States. The States live in the hope that the next award of the Finance Commission would bring forth some relief to their finances. Such fond hopes deaden their own efforts to mobilise resources. This is very much apparent from the trends we have seen in the state budgets presented in the legislatures this year. Barring one or two States, no State has undertaken any additional resource mobilisation simply because the Finance Commission's award is yet to come. The same tendency is reflected in the Centre, with its D.A. structure in which a rise is given effect to without considering the possible strains it would impose on the state finances. Any increase in D.A. affects general prices; stabilisation of prices is not within the sphere of the activities of the States. So when Centre incurs such expenditure the States have to be consulted. At present there is no mechanism by which States could be associated with such policies. I will, therefore, submit that on such questions as scaling down of debts, etc., a high level commission ought to be constituted and empowered to review what has happened during the last 20 years or so before recommending changes in the system and the basis of devolution. But it does not mean that the Central bill should be allowed to shrink to such an extent that it should not have the necessary resources to apply the correctives for removing the regional imbalances which have been created. It must have the necessary resources for directing planned development of the key sectors of national economy and it is the Centre and the Centre alone, that can take care of the special needs of border States like J & K, Assam, Nagaland, etc. All these aspects have to be taken into consideration by such a high powered commission.

On the question of rescheduling of the loans it is true that whosoever has taken a loan must pay it back. If loan-financed investments do not bring in adequate returns and consequently loans cannot be repaid or serviced some rethinking has to be done. While on the one hand the sanctity of loans ought to be maintained, on the other, the present burden of debt on the States, should be lessened through rescheduling of loans. The approach is bound to be different for different States. The Ministry of Finance has accepted the principle of rescheduling of loans and no one need fight shy of this. My submission is that there should be some scaling down of debt besides rescheduling of the rest. There is a suggestion to write off the unremunerative portion of the outstanding debt of the States and restrict central loan financing to productive schemes. These and other questions relating to the use of postal and small savings collection from States should also be examined by the proposed high powered commission.

LIC and Unit Trust should be persuaded to commit part of their funds to the state sector. It is suggested hopefully that a Finance Commission with a permanent secretariat could improve Centre-State financial relations. At one time we were told that the Finance Ministry will have a cell which will make certain research studies and keep records and data up-to-date about the finances. Such a machinery must be strengthened and preferred to a permanent Finance Commission which may involve a special process. At one time it was thought that we should have only one body. The Constitution itself provides for that—the Finance Commission. I think that the States should be associated with policy-making on problems of national importance and some mechanism has to be evolved to ensure such participation. The problem of resource mobilisation is important enough to be discussed at such high levels.

Dr. D. T. Lakdawala

As far as the Centre-State relations are concerned the first question that will arise is whether undue dependence of the States can be reduced and the best way to reduce such dependence would be by giving greater tax powers to the States. The other is whether one can think of any tax sources which can be transferred from the Centre to the States without reducing their

effectiveness. As far as I am able to see, by and large, I have not seen any such proposal in recent years which can enlarge tax powers of the States. On the contrary, both in this house and outside many proposals have been made for transfer of certain state powers of taxation to the Centre by an agreement or by constitutional amendment.

The question of the use of Article 269 has also been raised. I think difficulties in this respect have arisen, because the Constitution provides that this tax is to be raised by Centre but the proceeds should entirely belong to the States. The lacunae are : (*i*) who is to decide the rate of the tax, (*ii*) who is to decide when the tax is to be increased, and (*iii*) who is to decide when the tax is to be decreased. If these lacunae can be removed, it will be a great help. There is at least one tax, *viz*., estate duty, where the Centre has been vigilant but in other cases, the legitimate feeling in the States is that they should be consulted on the level of taxation.

Tax powers of the States cannot be increased. The best way is to evolve some mechanism for transfer of tax resources from the Centre to the States. In the Constitution it is looked after by a Finance Commission. More recently, the Planning Commission had been added. Obviously, there has been some overlapping in the functions of the two Commissions. The question from my point of view is not so much the transfer of resources to the States as their transfer in such a way that the resources are used most and effectively, and with a built-in progressivity. From that viewpoint, the fact that the Planning Commission has also been looking on the revenue side and that the Finance Commission has to look to the interest of the loans which have been sanctioned by the Planning Commission introduces an element of overlapping, which leads to the inefficient use of the resources.

Non-Plan capital budget, which concerns repayments by the States to the Centre, is a third matter which has to be certainly looked into. I would add a cave at here, that it is no use thinking of rescheduling of debts, much less, writing them off, unless we agree on the principle of interest. This may differ state-wise and purpose-wise. What are the purposes to be kept in view and what should be the interest rate that has to be charged

to each type of loan or each State ? Any effort at rescheduling or writing off will be fraught with grave dangers—unless we have a clear principle, and in my view, the only principle is how we are going to use these loans in the future.

Another question that has been raised is the amendment of the Constitution by having in it, provisions regarding how funds are to be divided. The difficulty in writing down such principles in the Constitution is that it makes procedures somewhat rigid. If you examine Finance Commission reports it is evident that at least in the past, the Finance Commission has been transferring some funds by way of tax devolution and the rest by way of grants. If this is going to be the pattern, writing down in the Constitution will make it rigid. If it is demanded at the same time that there should be a permanent Finance Commission to revise the system from year to year, how can the demand be taken seriously ?

Some demand has been made regarding greater transfers by way of postal savings, LIC funds and so on. I am really not competent to go into this question. There are one or two leading principles involved in this. The first thing is that a transfer of resources from one layer to another is worthwhile provided that the other layer can use it effectively. In the case of small savings, the States could help in greater mobilisation of resources. If this argument can be applied to other savings, it is all right. We are not asking for devolution of savings from one sector to another. As far as LIC and other bodies are concerned, the structural limitations under which each body operates, are known. There is some advantage in LIC loaning to the Centre and the Centre loaning to the States. Things can be done better by the Centre. The moment you demand a transfer of powers to the States, you will be confronted with the problem of regional imbalances. Concern has already been expressed about these imbalances and the way in which funds have been allocated in the past. One has to see the limitations under which such transfers are made. Planning Commission transfers are by consensus. In a consensus it is obvious that the States may not get all that they think are due to them. Already in the Finance Commission's formula, there is a large emphasis on population. As regards excise duty, 20 per cent

of it is distributed on economic considerations. Article 275 grants have gone to weaker states. They have not gone to the richer states.

When one talks of backwardness, one has to be very careful. All the past theories of backward regions on 10 per cent or 20 per cent criteria cannot work. When you have a definition by which 60 per cent of the country claims to be backward, I do not know what operational principles you can lay down. Backwardness cannot be improved by financial resources. It is a matter of what the backward regions are prepared to do themselves.

From the short-term point of view, backwardness may have a minimum rate of growth. A good deal of difficulties in the past has arisen because of the low rate of growth. You will have to make up your mind what value you want to attach to the equalisation of regional development. Further, all regions which are backward are not even in the long run capable of growth. There are regions which may need 50 years for self-sustaining growth while others only 15 years. Therefore, in any policy when we talk of economic backwardness or when we talk of policies of balancing them, we should bear in mind that it is the country as a whole which is backward. The total funds are, I am afraid, small indeed, considering the vastness of regional imbalances and also stagnation of the total economy which is running at a low level.

Shri R. C. Bhargava (J & K)

I have only two criteria to suggest. The whole question of Centre-State relations hinges on two factors : (*a*) states have been dissatisfied with the amounts of funds they get, (*b*) States feel that some States get more than the others. My point is that any change in the system of taxes can only be justified if it adds to the overall resources of the country as a whole. Merely a transfer from the Centre to the States does not solve the problem. We have also to see whether this transfer of the items from the Centre to the States will help in a more equitable distribution of resources. We have this phenomenon of a few States getting more, accentuating the problem of imbalances. It is by sharing that the Centre is able to get a large

distributive power. I do not think under the present system any change in the tax structure is possible and nothing can go from the Central list to the States.

Another point is about the need of the States in rescheduling the loans. Why has the problem arisen ? Having come to that, are we going to do anything so that this situation will not arise in future ?

About LIC loans, the only thing is that at present financial institutions do not give money for industrial projects which are financed by the State Governments. That policy should be changed because, otherwise, the Central financial institutions are not going to increase the financial assistance for the backward areas in the country.

Dr. D. T. Lakdawala

Regarding the question of increasing dependence of States on the Centre, it should be borne in mind that the economic assistance the Union Government obtains from foreign governments and agencies does bear some obligations of interest. In turn the Centre cannot afford not to charge interest when loans are advanced by it to the States.

Dr. Mathew Kurian

I personally do not agree that it is not within the range of possibilities for the Central Government to set apart a substantial amount for the really backward states of the country. Unless this is done, the present difficulties—political or financial—will continue and will in course of time become worse. The NDC has at best given only insignificant weightage to the backwardness of states and that also depending on particular circumstances of the State concerned. The NDC must address itself to the question as to how to distribute the three thousand five hundred crores which have been decided to be distributed to the States by way of Plan assistance. The working paper does not come out with any concrete suggestions as to how the Constitution can be amended and as to how various items of taxation can be transferred to the States. It is, I think, amply clear and I think Dr. Lakdawala will also agree, that backward states are going to suffer rather than gain. That point should be carefully kept in view because we of the backward states are

not able to put up our case before the Finance Commission. More use should be made of Article 275 of the Constitution. The position is exceedingly difficult and a consensus might emerge on an amendment of the Constitution. Therefore, it is best to leave the matter to such constitutional commission as has already been provided for in the Constitution. It is also at the same time true that over the years none of the Finance Commissions has so far been able to deliver the goods. I have to make suggestions or recommendations which would effectively give more weightage to the backward areas of the country. And it is only through such bodies as the Finance Commission that a greater part of the resources can be set aside for the really backward states. Dr. Lakdawala's point that there are backward states everywhere needs to be slightly modified. The qualification is this that if in a state which is more advanced there are yet backward areas which require attention in regard to assistance it should be that the prosperous state should take care of its backward areas and not the Centre. All the States should do likewise. That point has to be borne in mind, otherwise there is going to be a lot of confusion. NDC may also be seized of this point. We are talking in terms of financial resources of administrative units like States or the Centre. It should be made the responsibility of that political entity which has larger resources at its disposal to take care of its backward administrative or political unit. Some help of course should necessarily be given but there must be some effective weightage in favour of backward areas which do not have the resources at their disposal.

Dr. Y. S. Parmar

This is a matter of great controversy.

Shri R. H. Mehta (Gujarat)

This morning Mr. Pitambar Pant said that he had carefully studied the constitutional provisions and he found that there were no difficulties in the States raising enough revenues on their own. Our difficulties are not constitutional. Our difficulties are more practical. Those States which go in for additional taxation are bound to lose. This is because of the practice followed by the Planning Commission up to at least

the third Plan in covering the gap between the resources and the plan by means of Central assistance. To some extent this has been corrected by the various criteria that have been approved by the NDC and it was more or less as a result of what we said that at least 10 per cent incentive is given to the States going in for larger taxation. On the other hand, 60 per cent weightage is still being given to population. When we are laying so much emphasis on family planning, is there any point in giving weightage to the extent of 60 per cent on population ? Although I would say to some extent the Planning Commission has considered our point, the Finance Commission has not adopted this so far. They always go by the revenue gap and give Grants to those States which become extravagant. No norms have been set up by the Finance Commission.

We are talking of buoyancy in sales tax. Nobody has tried to work out as to how much of this is due to price rise. For the last few years prices have been going up and increased receipts from sales tax are there largely due to increase in prices. So sales tax revenue is bound to go up to the same extent.

A point is made that there is no great scope for further taxation especially in agriculture. It is well known that in the absence of large plantations, there is very little scope and we know from our experience that even if agricultural income tax is levied, our receipts in this regard are not going to be more than a few lakhs of rupees. Coming to the point of rescheduling of debts, to my mind, there is no case for rescheduling of debts. If we really go into the liability of the State Governments we will find that some of the grants of the Government of India are in fact loans to the State Governments. This is often forgotten completely. In other words it means that the loans which are received by the States are grants-in-aid by the Government of India.

Dr. Y. S. Parmar

And what about the interest ?

Shri R. H. Mehta

The same interest which the Government of India pays in the case of loans may be charged from the State Governments.

If all these debts which are incurred by the State Governments are eliminated, then I agree that there is no rescheduling of debts.

Dr. D. T. Lakdawala

All that I said was that rescheduling of debts should be linked with repayment. I never said this should or should not be done.

Shri R. H. Mehta

If we are given loans equal to two-thirds of the net collection as in the case of postal savings, where is the question of repayment to the Government of India ? The question does not arise at all. We have been pressing this point with the Government of India. If the Government of India agrees to repay the debts to the public from their own funds, then the question of rescheduling of debts should not arise. My point is that we should not press too much for rescheduling of debts, provided correct assessment of the loans granted by the Central Government to the State Governments is made.

Some of the speakers have spoken of Article 269 of the Constitution. I think these are the taxes which are available to the State Governments. We have only two taxation measures under Article 269. Supposing tax is levied on sale and purchase of magazines and newspapers. It means considerable revenue to the State Governments. So is the case of newspaper advertisement.

I do not think anybody has touched on stamp duty on Central items like promissory notes, cheques, insurance policies so far. These rates have remained static for a number of years. By raising the rates, resources for development will be available to the State Governments. Similar is the case of excise duty. I do not say that these sources may be given back to the State Governments. But I would definitely say that the rate of taxation should be reviewed periodically and made *ad valorem* so that when there are higher prices we get more through taxation measures.

There is another point on which nobody seems to have touched so far and that is that out of the total receipts of income

from taxes more than 50 per cent is received by way of corporation tax. The State Governments get nothing out of the surcharges on income tax. In effect, the State Governments get only about 23 per cent of the total collections from income tax, corporation tax and surcharges which become the divisible pool.

III. Mobilisation of Resources from Agriculture

(Chairman : Dr. Y. S. Parmar, Chief Minister, Himachal Pradesh)

Dr. Y. S. Parmar

We have had a very useful discussion on Centre-State financial relations. Very useful information has been given. Now let us take up the matter of mobilisation of resources from agriculture. The main points for discussion are raised on page 74 in the working paper.

Shri S. K. Govil (Planning Commission)

I may be permitted to say that mobilisation of resources from agricultural sector is a very key issue. Agriculture accounts for nearly half of our national income. Consequently, if the contribution of agricultural sector is not of a reasonable order, then I am not sure how fast and how far we can go in financing development.

Now so far as the means of mobilisation are concerned, the weapons in our armoury are, land revenue, agricultural income tax, various kinds of cesses, irrigation rates and so on. In addition, there are some other instruments of mobilisation such as loans, small savings, rural debentures and so on.

Land revenue is an old tax. But it has been somewhat static and regressive. I think it is useful to introduce elements of progression in rural taxes. Certainly we ought to introduce progressive agricultural income tax. So far an element of progression has been attempted in land taxation through surcharge on land revenue. But this can help only to a limited extent.

The other thing is irrigation rate. As it was mentioned it is just a fee for services rendered and there is no reason why it should not be adequate to recover the cost.

In my view rural debentures can make a major contribution as a self-financing method in agricultural development. I think the policy of subsidies to agriculture should be withdrawn. I think most of the friends have accepted the point that there is considerable scope for mobilisation of resources by the States and I agree with Dr. Lakdawala that each State should have its own tax structure. But in the present situation there are definite limitations. Take for instance the problem of uniform sales tax in the Southern region. They find it very difficult to implement such decisions taken in the regional councils. Planning Commission has exhorted them to adopt uniformity in sales tax. But there are political difficulties. This is also true in the case of electricity rates where States find it difficult to evolve a mutually agreed rational tariff structure.

Shri S. P. Sukla (Bihar)

I generally agree with the approach outlined by Shri Govil and I only want to say that whatever may be the theoretical consideration regarding progressive elements to be introduced in any tax on agriculture, there is the purely political demand that we should give up what we have already had. In terms of quantities, for example, in my State of Bihar the highest collection we have shown on agricultural income tax has not exceeded 18 lakhs a year which means that if we were to substitute agricultural income tax for land revenue, then we ought to increase its yield by 50 times and I do not think it will be possible in the foreseeable future. Bihar is also having problems about irrigation rates. Our present rates are only Rs. 16 per acre for kharif. This is particularly low in an area like Purnea. There is scope for increase. But there is certainly a political difficulty and the atmosphere has been so created that any talk of continuing land revenue itself has become an anathema. I suggest that we should recognise this and perhaps it is the duty of the intelligentsia of the society to put forward this in a very frank manner disregarding political pressures.

Himachal Pradesh Representative

The problem of collecting resources from the agricultural sector is a problem which touches the whole fabric of our society. At least 90 per cent of our population live in the villages

under conditions which are entirely different from those prevailing in the cities. We have a certain elementary structure of rural taxation in the form of land revenue, betterment levy and irrigation levy and some of the State Governments have made an effort to levy agricultural income tax. I was surprised to hear from the distinguished members that the rate of taxation could be equalised with the income tax in general. Probably, they kept the urban point of view before them when they made this suggestion. Who is the person whom it is going to touch ? It is going to touch a person who does not know rules and regulations and who is very much afraid of governmental machinery. If we are going to introduce this system of assessment, the system of levy, exemptions, and so on, we would be bringing the lawyers and pleaders into the life of the villagers. This will be a fundamental mistake, and a risky proposition. Once this system is introduced, there will inevitably be a further fragmentation of holdings and division of properties. We would also be introducing a system of hypocrisy and deceit in rural life. It is true that due to the efforts made in the last three plans, certain amount of income has been generated in the rural sector of the economy, which can usefully be tapped and put to the national use. But on no account, should agricultural income tax be brought on par with income tax. In Himachal Pradesh we propose to impose a tax on agricultural income bearing these difficulties in view. In assessing gross income, we have to take into account the market price, and the quantity of output. Determination of price is left to a committee wherein the representatives of agriculturalists are given a prominent place. This provision takes assessment out of the purview of the tax officials.

The second element in assessment is to determine the net profit which accrues to the farmer. We are not thinking of taxing income. We are thinking of taxing net profit. Profits fluctuate and we have to allow for it. It is the committee and not the tax authorities who will examine the various aspects of income, cost and net profit. This method is to spare the farmer a lot of harassment. Actually, the committee makes a liberal provision for cost. This is particularly helpful in view of the difficulties faced by illiterate farmers in maintaining a system of account acceptable to income tax authorities.

Besides agricultural tax, we levy entry tax on vehicles entering the State which is called, in other words toll tax. In addition, Himachal Pradesh taxes a large number of visitors. We want to attract as large a number of tourists to our State as possible. We want to attract more and more people and especially foreigners. A larger influx is already taking place. We would like to tap this source through two simple taxes—vehicle tax and entry tax. Every vehicle entering the State carrying passengers or goods will pay a particular rate of toll tax. This will be in lieu of the services which the State Government is rendering to persons who visit the Himachal Pradesh. This tax is borne by a strata of society which has the capacity to pay.

Shri K. S. Narang

How do you distinguish between visitors—that means you are also included ?

Himachal Pradesh Representative

Yes, certainly I am also included.

Dr. Y. S. Parmar

Anyway it is an experiment. Well I think we have had a very useful discussion on various matters and the last was tax on agriculture. I do not think I have much to wind up. I am getting more interest in this subject which has excited so much heat. It is very serious especially from the point of view of crisis through which the country is passing. The greater realisation is coming both from Centre and the States that unless steps are taken to properly look into that matter and find the resources we are going to be in trouble. As for transfer of resources from the Centre to the States, there is no denying the fact that the Centre can only distribute what it has. It is only within this constraint that this problem is to be approached.

But there is no denying the fact that by and large 75 per cent people depend on agriculture and in places like Kashmir 93 per cent depend on agriculture. And there is no agricultural income tax in Kahsmir.

A voice : That has been held in abeyance.

Dr. M. J. K. Thavaraj

Friends, it is my privilege to propose a vote of thanks. I will make just a few brief comments by way of winding up the discussions. When I proposed this Conference to Dr. Khosla, I could not claim any close intimacy with tax problems of States other than Kerala though I had comparative tax data at my disposal. I had no interest in projecting ideas of my Committee on others as I thought they would have serious limitations. But I am glad that the basic approach which we had in view is, by and large, vindicated through the discussions we had today.

Even though we have to look at the problem of mobilisation of the country we cannot help looking at the problems of the States. There are states where parties with orientations different from that of the Centre have come to power. We cannot tell them that they should be satisfied with whatever regressive tax systems they might have inherited. They are also popular governments elected on the basis of a particular programme and it would be their endeavour to look to the tax structure in accordance with their basic approaches to socio-economic problems.

Another thing which was peculiar to Kerala was that their land tax system was different from that prevailing elsewhere. There a land revenue is not a settlement tax. It is a basic tax of Rs. 2 per acre. It is protected by its inclusion in Seventh Schedule. They cannot therefore alter the rate. Any amendment proposed can be challenged in the Court and knocked down. But the land remains the main base of taxation in Kerala.

If as in other States, cesses or surcharges could be levied on land revenue, a portion of the increased incomes from agriculture could be mopped up. But the Committee was convinced that this by itself could not ensure equity between different classes of rural population. But in Kerala the land tax is so rigid that it is not possible to do so unless a land revenue system based on capital value is adopted along with agricultural income tax. This is also important if ability to pay is to be given due consideration in the tax system.

The other aspect which attracted our attention was the enormous element of subsidy involved in public expenditure as well as in the pricing policies of public utilities and other undertakings. We all agreed that by stages within the next 3 or 4 years the Kerala State Electricity Board should be able to declare 11 per cent return on its capital. The Government of Kerala has also agreed to review its policy of subsidies paid to the various segments of population.

We also found that commodity taxation in Kerala was very high and basically regressive in character. Therefore, we felt that it would be inequitable to have further increases in sales tax. We suggested that such increases may be restricted to comforts and luxuries though there are limits to such efforts arising from diversion of trade on account of inter-state disparities in rates. At the same time we paid a lot of attention to problems of evasion and improvement of tax administration to which this Conference could not devote adequate attention.

I would now like to convey my appreciation for the good response we had for this Conference. We expected some more Chief Ministers but they could not come. The Chief Minister of Himachal Pradesh, Dr. Parmar was kind enough to sit through the entire proceedings and I am grateful to him and also to all those who participated in the Conference.

I should also thank Dr. Khosla, the Director of the Indian Institute of Public Administration for the encouragement and support he gave me towards the organisation of this Conference. I also owe a lot to the Office of Training for their admirable work towards the successful organisation of this Conference. Once again I thank all those who participated in this Conference and enriched its proceedings.

ANNEXURES

I. LIST OF PARTICIPANTS

II. WORKING PAPERS

(1) Approach to State Taxation.

(2) Centre-State Financial Relations.

(3) Mobilisation of Resources from Agriculture.

III. (*a*) Paper on "Mobilisation of Additional Resources from the Agricultural Sector for the Fourth Plan".

(*b*) Extract from Chapter I of the Taxation Enquiry Committee Report of the Government of Kerala.

ANNEXURE I

LIST OF PARTICIPANTS

REPRESENTATIVES OF STATES AND ADMINISTRATIONS

Assam	..	Shri G.C. Phukan
Bihar	..	Shri S.P. Shukla
Gujarat	..	Shri R.H. Mehta
Haryana	..	Mrs. Om Prabha Jain Shri M.L. Batra
Himachal Pradesh Administration	..	Dr. Y.S. Parmar and Officials
J & K	..	Shri R.C. Bhargava
Kerala	..	Dr. Mathew Kurian Shri S. Padmakumar
Madhya Pradesh	..	Shri R.N. Malhotra
Maharashtra	..	Shri N.G. Abhyankar
Manipur Administration	...	Shri L. Soloon
Mysore	..	Shri Mani Narayanswamy Shri G.V.K. Rao
Punjab	..	Shri K.S. Narang
Tamil Nadu	..	Shri J. Shivakumar Miss M.S. Ramesh
Uttar Pradesh	..	Shri N.D. Tiwari Shri A.R. Siddique
West Bengal	..	Shri J.L. Kundu Shri B.C. Ganguli

PLANNING COMMISSION

Dr. D.R. Gadgil
Shri Pitambar Pant
Shri B. Venkatappiah
Shri S.K. Govil

OTHERS

Dr. D.T. Lakdawala
Dr. S.R. Sen

INDIAN INSTITUTE OF PUBLIC ADMINISTRATION

Dr. J.N. Khosla
Prof. N. Srinivasan
Prof. G. Mukharji
Dr. V. Jagannadham
Dr. M.J.K. Thavaraj
Dr. S.R. Maheshwari
Shri A. Datta

ANNEXURE II

Working Papers

SESSION I

APPROACH TO STATE TAXATION

Indian Union comprises states and regions of extreme diversities in size, density of population, historical and cultural heritage, natural endowments as well as social and economic development. Regional disparities in the pre-British period were mainly attributable to historical and natural factors. But the commercial and industrial developments that characterised the British period (especially during the last hundred years) aggravated the lopsided development of the different regions. Recent developments have not materially altered this trend. A measure of such regional disparity is the wide difference in the per capita income of the different States. The anxiety of the poorer States to overcome their backwardness in development can easily be understood. But the mechanism for mobilisation, allocation and transfer of resources has not been quite conducive to a progressive redistribution of regional disparities.

As in most other federations there is a growing divergence between the responsibilities arising from the original distribution of powers and fiscal capacity between the Union and State Governments in India especially under the weight of successive Plans for economic and social development. As it has come to be the Centre is concerned with the most generalised features of the national frame (such as the creation and maintenance of the credit and monetary system, railways and ports, as well as the facility for national economic planning) and with highly concentrated actions at a few strategic points (such as the regulation and development of large-scale industries, exploitation of mineral resources, state trading, regulation of foreign trade, etc.). On the other hand, the States are concerned with acting on the total life of the people transmitting the forces impelling

economic development of all areas and units as well as with concretising the fruits of development to all the individuals within their territories. Infrastructure investments such as irrigation, power and regional and local roads as well as the outlays on human resources through the development of educational and health facilities are the responsibilities of the States. The generation of income and employment largely depends on the extent to which the State Governments could promote the primary industries such as agriculture, forests, fisheries, mining and the secondary activities in the small and medium industries apart from conserving traditional handicrafts.

In fulfilling these developed responsibilities the States have become increasingly dependent on the Centre for their current as well as capital resources. The fiscal dominance of the Centre over the States could not bring about balanced regional development. Nor has the Centre used other instrumentalities at its disposal to narrow down the unevenness in regional development. Even the network of banking and other financial institutions has largely helped to transfer resources from the relatively poorer to the richer areas. Hence, it is often demanded that the existing fiscal arrangements may have to be altered so as to augment the free resources of the States, to scale down the indebtedness to manageable proportions and to transfer adequate resources to the poorer States.

The existing arrangement seems to have assigned a more favourable tax base to the Centre. Under the existing scheme of distribution of tax powers relating to property, land constitutes the main base for state taxation whereas taxation of industrial and commercial property is the preserve of the Centre. In a densely populated country the volume of land assessable to tax remains almost static. Therefore, land as a source of revenue would largely depend on enhanced rates on the one hand and enlarged agricultural income on the other. In contrast, the step up in the pace of industrial development under the Plans has meant a tremendous expansion in the base of industrial and commercial property and the income and wealth arising therefrom. This seems to have given a buoyancy to the central revenues which is not available to any tax head assigned to the States.

Commodity taxation is a field which is jointly being exploited by the Centre and the States. In this customs duties are a central prerogative. So are the excise duties except those levied on alcoholic liquor and narcotics. There is already a ceiling on the rates on inter-State sales. Some commodities subjected to additional excise duties in lieu of sales tax seem to be suffering from neglect. These restraints along with the need to move in harmony with the neighbouring States seem to give the Centre an edge over the States in commodity taxation except in those States where industrial and commercial activities are concentrated. The scope for raising sizable revenue through registration, motor vehicles and other taxes is clearly limited.

States which would like to pursue the social objectives enshrined in the Directive Principles of State Policy and elaborated in the earlier Plan documents along with their efforts to mobilise additional resources to meet the requirements of planned development are severely constrained in a number of ways. Except in land the States cannot alter property relations. Nor are they armed with instruments of control and regulation to alter the structure of production. Within these constraints a simultaneous search for more resources and greater progressivity within the existing framework is beset with a lot of difficulties. The search for one is likely to endanger the pursuit of the other. For instance, any shift from consumption-oriented to property or income-oriented tax structure may be conducive to greater progressivity in the system. But unless land-based taxes are made steeply progressive it is not likely to bring in a substantial increase in revenue.

The dilemma between increased production and equitable distribution of the burdens of resource mobilisation becomes more real when the State Governments assume the role of an underwriter of development efforts within their respective territorial jurisdiction. Apart from loss of revenue such an underwriter's approach to the development of the state economy tends to introduce an element of regressivity into the tax system. At the same time it would be difficult to ignore the role of the State as a promoter and underwriter of development so long as inter-State rivalries and the bargaining power of the investors remain as they are.

Landed property confirms several advantages on the owner. Apart from psychic income arising from power, prestige, security and so on, land confers real economic advantages through income, rent, capital gains, etc. Part of this is unearned. Consequently the landowners stand on a privileged position vis-a-vis the large number of landless peasants, urban workers and even a large section of urban workers and salaried groups. In recent years non-agricultural lands in the urban areas, more than agricultural lands have registered an unprecedented appreciation in value on account of the rapid pace of urbanisation. Speculation in land has given a tremendous boost to land values. Considerable resources have flown into the urban sector by way of investment in land and other assets. On the other hand, land use has become the crucial factor in town planning. Mere taxation of land will, therefore, be far too inadequate in dealing with the complex problems of planned urban development. Only a carefully worked out programme of land nationalisation coupled with suitable measure of land taxation appears to be the real answer to the problems created by speculative dealings and unplanned use of urban land.

As for land taxation, the search is for a new basis combining the characteristics of productivity, equity, flexibility, progressivity and simplicity and make land contribute its due to the state exchequer. Land revenue based on cadastral survey and settlement has proved to be regressive and static. But insofar as the results of capital improvements, infrastructure facilities and the pressure of population on land would be adequately reflected in the capital value of land, such a tax might offer a flexible basis for a progressive tax on land provided a machinery could be created for periodic revision of the capital value of land. Agricultural income provides a facile base for progression in the rates of taxation though most of the States have taken to it somewhat grudgingly. With appropriate differentiation in the rate between personal and company incomes on the one hand and the domestic and foreign companies on the other, agricultural income tax could serve as one of the most progressive taxes in the fiscal kit of the State Governments.

Points for Discussion

(1) How far is it possible to adopt a progressive tax policy

which would shift the emphasis from a commodity-based to a progressive and flexible group of taxes designed to tap more intensively land and income and wealth arising therefrom ?

(2) In what ways could the role of the States as a promoter and underwriter be reviewed so as to prevent shifting of resources from the relatively poorer tax payers to the affluent investors and producers (*e.g.*, subsidised electricity tariffs and subsidised inputs in agriculture) ?

SESSION II

CENTRE-STATE FINANCIAL RELATIONS

Of the total expenditure of States (Plan and non-Plan) excluding the discharge of repayment of debt, the resources from the Centre have increased from 42 per cent in the First Plan to 49 per cent and 52 per cent respectively in the Second and Third Plans. More than 53 per cent of the total resources transferred consist of loans. Of the balance more than half is attributable to grants-in-aid (revenue and capital) the remaining being States' share of divisible taxes. The relative share of statutory grants has suffered a striking decline over the Plans and during the first fifteen years of Planning discretionary grants were more than twice as large as statutory grants. The same trend seems to have continued since then. Such a striking dependence seems to be the natural consequence of the enormous command enjoyed by the Centre over relatively larger and larger revenue resources mobilised through the fiscal systems besides those available from banks, insurance, foreign trade and assistance, postal deposits and other sources of non-tax revenue.

Such a command over resources has not brought about the requisite transfer of resources to reduce inter-regional disparities. The Annual Survey of Industries reveals wide inter-State disparities in industrial development. There are also very wide variations in per capita bank deposit and per capita bank credit in the States. By and large the richer States seem to have absorbed a predominant part of the resources channelled through the financial institutions in India. Even the regulation and control over industrial development has not proved to be effective instrument in mitigating regional disparities in development. No consistent principle governing locational decisions regarding Central investments is discernible.

There are several specific complaints from the States such as that :

(1) The amalgamation of the tax on railway fares with the ticket fares has worked to the disadvantage of the States.

(2) The Centre has not shown sufficient enthusiasm or initiative in exploiting for the benefit of the States all the taxes enumerated in Article 269 of the Constitution.

(3) The Centre is not very much interested in tapping more intensively commodities entrusted to the Centre for the levy of additional excise duty in lieu of sales tax.

(4) The Centre has made occasional inroads into the divisible pool through such practices as :

   (*i*) resorting to surcharges on income tax ;

   (*ii*) by declaring income tax paid by the companies as corporation tax.

(5) The Concurrent List has proved to be a vehicle for powers to gravitate towards the Centre.

Points for Discussion

(1) In what ways could the fiscal arrangements between the Centre and the States be altered to augment the free resources of the State; to scale down the indebtedness to manageable proportions; and, to transfer adequate resources to the poorer States so that they may have enough elbow room to adjust their plans to suit their own peculiar circumstances and fill the gaps in their development and to catch up with the more advanced States in the Union ?

(2) Whether it is desirable to constitute a high-powered Commission to review the various constitutional issues and practices affecting Centre-State relations ? Or whether as recommended by the ARC Study Team Report on Centre-State Relations a Special Finance Enquiry Commission could be constituted to examine the question of widening the base of devolutions and of prescribing the share of divisible taxes in the Constitution itself ? Could the Centre's role in Concurrent and State subjects be brought within the purview of such a Commission ?

(3) Whether it is feasible to write-off the unremunerative portion of the outstanding debt of the States and restrict central loan financing to productive schemes ?

(4) Whether it is possible to allow the entire amount of the postal and small savings collection from a State to be used in the State for productive schemes ?

(5) Whether LIC and Unit Trust could be persuaded to be more liberal in their lending policies to the State Governments and their undertakings?

(6) Whether a permanent Finance Commission with a permanent Secretariat could improve Centre-State financial relations ?

(7) In what ways could the NDC be strengthened and developed for high level decision-making on all issues of national importance in planning and policy-making for development?

(8) Is it possible to evolve a code of ethics governing the Centre-State financial behaviour ?

MOBILISATION OF RESOURCES FROM AGRICULTURE

Though taxation of land relates to both agricultural and non-agricultural land the problem is generally discussed with special reference to the agricultural sector. The case for mobilisation of additional resources from this sector would depend upon the extent to which the income or surplus generated in this sector is tapped. The implementation of the Five Year Plan has resulted in a progressive step-up in public outlays in the agricultural sector. Under the First Plan the outlay was Rs. 600 crores for the country as a whole; it rose to Rs. 980 crores under the Second Plan and further to Rs. 1,718 crores under the Third. But the studies made by the Planning Commission have revealed that in 1950-51 the agricultural sector paid only Rs. 186 crores in taxes while it received Rs. 286 crores out of the current expenditure of the Governments. On the other hand, the non-agricultural sector paid Rs. 391 crores in taxes and received only Rs. 286 crores. The net flow of funds into the agricultural sector has considerably increased over the Plan period. In 1961-62 the agricultural sector received Rs. 781 crores from the current budget of the Governments while it paid only Rs. 413 crores by way of taxes.

Income from agriculture increased from Rs. 4,780 crores in 1950-51 to Rs. 10,930 crores in 1966-67. The agriculturists in general have benefited not only from increases in farm productivity but also from favourable market conditions. The bulk of the benefits that have accrued to this sector has, however, gone to a small section of well-to-do farmers who on account of their position of vantage and by their political pulls and pressures have been able to annex a significant portion of the aids and subsidies offered by the Government.

The following observations have been made in the Planning Commission's note to the NDC :

"Indicative of the unequal distribution of income in the agricultural sector about 3/5th of the increase in the

agricultural income in recent years accrued, it is estimated, to farmers having 10 acres or more of land. These well-to-do farmers who account for nearly 61 per cent of the total operational area and belong to about 15 per cent of the rural household, it is obvious, also get the bulk of benefits arising from the facilities provided in the form of better seeds, subsidised fertilizer and pesticides and loans and subsidies for other purposes."

There are several studies which have revealed the enormous tax potential still remaining untapped from this sector. At the same time it is held that in view of the pressure of population on land and the tendency to redistribute land amongst the members of the family the potential for progressive taxation is not as much as it is sometimes imagined. Nevertheless, one has to pay adequate attention to the differing ability to pay of the various strata of agricultural population while dealing with problems of resource mobilisation from the agricultural sector.

Points for Discussion

(1) Will the existing framework of land taxation having various types of land revenue based on cadastral survey, betterment levy, irrigation cess, etc., be adequate to mobilise the additional resources from agriculture ?

(2) How far is it feasible to adopt a tax based on the capital value of land ? (It is now obvious that such a tax is within the legal competence of the States under Entry 49 of the List II).

(3) What kind of valuation machinery will be necessary to determine capital value of land from time to time on a State-wide basis ? Will such a valuation also help registration, stamp duty, wealth tax and so on ?

(4) Why can't the agricultural income rates be brought on par with the central income tax rates ?

(5) How could the States be enabled to collect an additional tax by aggregating agricultural and non-agricultural incomes?

(6) What is the scope for agro-industrial debentures in the States?

(7) What are the special problems in collecting irrigation rates and betterment levies ? In what way could these problems be solved ?

ANNEXURE III

A. MOBILISATION OF ADDITIONAL RESOURCES FROM THE AGRICULTURAL SECTOR FOR THE FOURTH PLAN

THE CASE FOR ADDITIONAL RESOURCES

Since the commencement of planning for development, public outlay has been considerably increased in the agricultural sector. Under the First Plan, the outlay amounted to Rs. 600 crores. It rose to Rs. 980 crores under the Second Plan and further to Rs. 1,718 crores under the Third. Besides, sizable expenditures, benefiting the agricultural sector, have been incurred on rural electrification, small-scale industries, social services and transport and communications.* Alongside this, income from agriculture increased from Rs. 4,780 crores in 1950-51 to Rs. 10,930 crores in 1966-67. Indicative of the unequal distribution of income in agricultural sector, about three-fifths of the increase in agricultural income in recent years accrued, it is estimated, to farmers having ten acres or more of land. These well-to-do farmers, who account for nearly 61 per cent of the total operational area and belong to about 15 per cent of the rural households, it is obvious, also got bulk of the benefits arising from the facilities provided in the form of better seeds, subsidised fertilizers and pesticides and loans and subsidies for other purposes. It is, therefore, only fair that the agricultural sector, particularly its well-off section, should contribute a reasonable proportion of its income to expanding public outlay in general and on agriculture in particular.

There are, besides, certain important considerations of fact as well as policy for adopting measures to raise larger resources than in the past from the agricultural sector, in particular, from the well-to-do section there. To state briefly, the considerations are:

(*i*) The agricultural sector, particularly its upper classes, have remained very much under-taxed as compared to the non-agricultural.

*For these, separate figures of outlay are not available.

(*ii*) The terms of trade between the agricultural and non-agricultural sectors have been changing in favour of the former, increasing in consequence its tax-paying capacity.

(*iii*) There has been a persistent flow of resources to the agricultural sector from the non-agricultural when the developmental needs of the latter are no less pressing than that of the former.

(*iv*) An increase in tax burden on the agricultural sector can not only arrest the decline in the marketable surplus of foodgrains but also ensure higher productivity in agriculture as a whole.

INTER-SECTORAL DIFFERENCE IN TAX BURDEN

The Taxation Enquiry Commission, 1953-54, making the first and a systematic study of tax incidence in this country[1] brought out the relative under-taxation of the rural sector. But, in the absence of any classification of population by income levels, the study was restricted to indirect taxes,[2] and it related tax payment to consumer expenditure (cash and non-cash) as indicated by the National Sample Survey. The study showed that in 1953-54 in the incidence, *i.e.*, direct money burden of Union and States indirect taxes was absolutely as well as relatively to consumer expenditure very much lower in the rural sector as compared to the urban. While the absolute tax burden on the rural sector at Rs. 0·62 on a per capita per month basis was nearly one-third of that on the urban sector, as per cent of consumer expenditure it was just half at 2·9 per cent. Over the subsequent five years to 1958-59, the incidence of Union and State indirect taxes on either sector increased substantially. But the relative burden of indirect taxes on the rural sector diminished somewhat. This was revealed in a study made by the Ministry of Finance and similar to that of the Taxation Enquiry Commission in methodology and coverage[3].

[1]Government of India, *Report of the Taxation Enquiry Commission*, 1953-54. Vol. 1.

[2]Central excise, import duties, state excise, sales tax, general and on motor spirit, entertainment tax, inter-State transit duties, sugarcane cess and motor vehicles tax.

[3]Ministry of Finance, *Incidence of Indirect Taxes*, Tax Research Unit, Department of Economic Affairs.

The absolute money burden of indirect taxes on the rural sector at Rs. 0·93 per capita per month was, as in 1953-54, nearly a third of that on the urban sector, but as per cent of consumer expenditure it turned out to be a little less than half at 4·4 per cent as against 9·3 per cent in the urban sector.

TABLE I

Incidence of indirect-taxes (all household)

	Taxation Enquiry Commission Study (1953-54)		Ministry of Finance Study (1958-59)	
	Rural	*Urban*	*Rural*	*Urban*
Tax per capita per month (in rupees)	0·59	1·62	0·93	2·70
Tax as per cent of consumer expenditure	2·9	5·1	4·4	9·3

Dr. K.N. Raj, in an article, "Resources for the Third Plan—An Approach",[4] extended the study of tax incidence to direct taxes. He allocated both direct and indirect taxes collected by the Union and State Governments in 1952-53 and 1957-58 to the rural and urban sectors on the basis of a rough approximation. However, his analysis shows that :

(1) during the period 1952-53 to 1957-58, the rural sector was considerably under-taxed as compared to the urban, tax as per cent of income in the rural sector having been about one-third of what it was in the urban sector;

(2) the increase in tax revenues since 1952-53 had been realised more from the urban rather than the rural sector; and

(3) while government taxation had probably absorbed nearly 40 per cent of the increase in income in the urban sector, the share of the Government in the increased income of the rural sector had been perhaps not more than 15 per cent.

[4] *The Economic Weekly*, Annual Number, January 1959.

TABLE II

Approximate share in national income and tax payment according to Dr. K.N. Raj

(Rs. in crores)

	Rural			Urban		
	1952-53	1957-58	Increment (2—1)	1952-53	1957-58	Increment (5—4)
	1	2	3	4	5	6
National income	6,850	7,900	1,050	2,980	3,500	520
Tax payment	289	430	141	386	576	190
Tax as per cent of income	4·2	5·4	13·4	13·0	16·5	36·5

Following the method of estimation adopted by Dr. K.N. Raj, the National Council of Applied Economic Research have computed the tax payment by the rural and urban sectors till 1964-65.[5] The computed figures show that between 1956-57 and 1960-61, while the income of the rural sector increased by Rs. 1,747 crores, tax payment by the sector increased by Rs. 183 crores. The marginal tax rate, (*i.e.*, increase in tax payment as per cent of increase in income) for the sector thus worked to a little over 10 per cent. On the other hand, during the same period, while the income of the urban sector rose by Rs. 1,143 crores, tax collection from the sector went up by Rs. 283 crores, giving a marginal tax rate of 24 per cent. The spurt in tax revenue and taxation in the wake of the Chinese invasion in 1963-64 caused sizable increase in tax burden for both sectors. The rural sector's contribution rose from Rs. 578 crores in 1960-61 to Rs. 915 crores by 1963-64 and that of the urban sector from Rs. 777 crores to Rs. 1,398 crores. But the ratio between the marginal tax rates of the two sectors did not alter much. The rural sector's income increased in this period by Rs. 1,629 crores and its tax payment by Rs. 337 crores, giving a marginal tax rate of a little over 20 per cent. The urban sector's income, on the other hand, increased by Rs. 1,481 crores and

[5]Planning Commission, *Financial Resources for the Fourth Plan* (Mimeograph).

tax payment by Rs. 621 crores, showing a marginal tax rate at 42 per cent.

TABLE III

Additional income of and tax payment by the rural and urban sectors according to the NCAER study

(Rs. in crores)

	Rural Sector			Urban Sector		
	Additional Income	Tax	Marginal rate of tax (%)	*Additional* Income	Tax	Marginal rate of tax (%)
	1	2	3	4	5	6
Between 1956-57 and 1960-61	1,747	183	10	1,143	283	24
Between 1960-61 and 1963-64	1,629	337	20	1,481	621	42

A detailed and sophisticated assessment of the relative burden of Union and State direct and indirect taxes on the agricultural and non-agricultural sectors has been made by Ved P. Gandhi,[6] covering the period, 1950-51 to 1961-62. His findings are as follows :

(1) In 1950-51, the agricultural sector paid only Rs. 186 crores in direct and indirect taxes, whereas the non-agricultural sector paid Rs. 391 crores. In 1961-62, the difference between the two became extremely large, the agricultural sector paid Rs. 381 crores and the non-agricultural sector Rs. 1,095 crores. Thus, whereas in 1950-51 tax payment by the agricultural sector was about half of that by the non-agricultural sector, in 1960-61, it became one-third.

(2) The agricultural sector paid about 3.6 per cent of its income in taxes in 1950-51, when the non-agricultural sector paid 8·8 per cent of its income. The average tax rate in the agricultural sector was thus less than half of that in the non-agricultural sector. The relation was the same in 1961-62; the agricultural sector paid

[6] *Tax Burden on Indian Agriculture*, Harvard Law School.

5.9 per cent of its income, and the non-agricultural sector paid 13.2 per cent of its income.

(3) Between 1950-51 and 1961-62, while the non-agricultural sector paid 20.6 per cent of its additional income in taxes, the agricultural sector paid only 11.6 per cent. This implies that the non-agricultural sector carried almost two-thirds of the burden of additional taxation for planned economic development, while the agricultural sector bore only one-third of the burden.

(4) The inequality in per capita taxes in the two sectors was also extremely large. In 1950-51 the per capita taxes in the agricultural sector were only Rs. 8 as against Rs. 36 in the non-agricultural sector—*i.e.*, the relative tax payment (per capita) by the non-agricultural sector was four and a half times that in the agricultural sector. In 1961-62, the inequality widened to five and one-third time; the per capita taxes in the agricultural sector were Rs. 14 as against those of Rs. 75 in the non-agricultural sector.

(5) Even if allowance is made for subsistence income to derive taxable income in either sector, the comparative under-taxation of the agricultural sector on a per capita basis is still revealed. In 1950-51, the per capita taxes in the non-agricultural sector were four and a half times those in the agricultural sector, while the per capita taxable income in the former was no more than twice that in the latter. Even in 1960-61, the picture was unchanged; the non-agricultural sector paid five and a third times the taxes per capita of the agricultural sector, while having per capita taxable income only three and a half times that of the latter.

The following table, giving Ved P. Gandhi's figures, indicates that despite a narrowing of the inter-sectoral disparity in per capita tax rates over the period, 1950-52, the per capita tax rate in the agricultural sector was three-fifths as compared to the non-agricultural sector in 1961-62.

Ved P. Gandhi further shows that if wealth per capita, income inequity and wealth inequity are also taken into account,

in addition to taxable income per capita[7], the conclusion of the relative under-taxation of the agricultural sector remains unimpaired. For between 1950-51 and 1960-61, as the table below shows, the relative per capita taxable capacity of the agricultural sector on this basis declined less than its relative per capita tax payment.

TABLE IV

Per capita taxable income of and tax payment by agricultural and non-agricultural sectors*

	Agricultural			Non-agricultural		
	Per capita taxable income (Rs)	Per capita tax (Rs)	Rate of Tax (%)	Per capita taxable income	Per Capita tax (Rs)	Rate of tax (%)
	1	2	3	4	5	6
1950-51	72	7·7	10·7	141	36·2	25·7
1961-62	87	13·6	15·6	197	75·2	25·3

*Per capita income minus subsistence allowance at Rs. 140 and Rs. 270 per annum for the rural and urban sectors respectively for the whole period.

TABLE V

Relative per capita income of and tax payment by agricultural and non-agricultural sectors

Ratio of Agricultural : Non-Agricultural—1	1950-51	1960-61
Income[8]	0·46	0·43
Tax payment	0·21	0·19

Ved P. Gandhi allocated the revenue from indirect taxes, which over the period since 1950-51 increased relatively more than that from direct taxes, on the basis of his judgment. His allocation, if compared with that effected by the Taxation

[7]Gandhi has attached varying weights to the four factors—per capita taxable income, wealth per capita, income inequity and wealth inequity.

[8]The agricultural to non-agricultural income ratio is based on one set of weights to the four factors in taxable capacity.

Enquiry Commission 1953-54 and the Tax Research Unit in the Ministry of Finance on the basis of consumption expenditure, appears to have placed an unduly greater burden on the non-agricultural sector. An attempt has, therefore, been made here to allocate the revenue from practically all Central and State direct and indirect taxes[9] in 1953-54, 1958-59 and 1965-66 to the agricultural and non-agricultural sectors on the basis of the findings of the Taxation Enquiry Commission and the Tax Research Unit of the Ministry of Finance in respect of the years 1954-55 and 1958-59 and studies relating to sector-wise distribution of income. The results reproduced in the following table show that relative under-taxation of the agricultural sector, though not as much as Gandhi's study would suggest, is undoubtedly there. Over all the years covered, tax burden on the agricultural sector relatively to its income amounted to a third less as compared to the non-agricultural sector. In the context of resource mobilisation, moreover, the relevant comparison, it may be maintained, cannot be between the agricultural sector and the non-agricultural sector, the latter including the non-agricultural rural sector which, by and large is functionally dependent on the former, but between the agricultural sector and the industrial-cum-commercial sector, *i.e.*, roughly, the urban sector. Such a comparison if it could be made[10] would show relatively greater under-taxation of the agricultural sector than is shown by the figures given in the table. The non-agricultural rural section is the least taxed by virtue of its means and general level of earnings; and if it is taken out of the non-agricultural sector, the relative tax burden on the organised industrial-cum-commercial sector will be seen to have been higher still as compared to the agricultural sector.

INTER-SECTORAL, INTER-CLASS DIFFERENCES IN TAX BURDEN

No less significant than the relative under-taxation of the agricultural sector is the prevalence of considerable under-taxation of the upper-agricultural classes compared to the upper-non-agricultural classes. The Taxation Enquiry Commission

[9]All except export duties, registration fees, stamp duties and minor taxes like tax on movement of goods.

[10]In the absence of relevant income estimates, such an inter-sectoral comparison could not be made here.

showed that in 1953-54 at all levels of consumer expenditure the burden of Union and State indirect taxes, absolutely as well as relatively to consumer expenditure, was lower for all rural as compared to urban households. It further showed that the inter-sectoral difference in favour of the rural sector was the greatest in the top household expenditure class (Rs. 300 and

TABLE VI

*Tax burden on agricultural and non-agricultural income**

		1953-54	*1958-59*	*1965-66*
1. Agricultural Income (Rs. crores)		5,200·0	6,089	9,080
2. Non-agricultural Income	,,	5,280·0	6,520	11,260
3. Direct taxes on (1)	,,	74·5	103·6	134·2
4. Indirect taxes on (1)	,,	185·9	326·2	855·9
5. Total taxes on (1)	,,	**260·4**	**429·8**	**990·1**
6. Direct Taxes on (2)	,,	164·4	237·0	594·1
7. Indirect Taxes on (2)	,,	218·9	405·3	1,157·4
8. Total taxes on (2)	,,	**383·3**	**642·3**	**1,751·4**
9. (5) as a per cent of (1)		5·0	7·1	10·9 (10·3)
10. (8) as a per cent of (2)		7·3	9·85	15·6

*Conventional series income figures.

After making allowance for the increase in land revenue due to the abolition of intermediaries.

Note : *Item 3 and 6—*

The revenue from wealth tax, gift tax and expenditure tax has been allocated to the two sectors on the basis of the ratio of the incomes of top farm and non-farm groups as given in a Reserve Bank of India article.

Item 4 and 7—

Assuming that agricultural population has the same pattern of consumption as rural population, the revenues from indirect taxes in 1953-54, and 1958-59 have been allocated to the agricultural and non-agricultural sectors using the per capita tax figures (given in the Taxation Enquiry Commission and Ministry of Finance, Tax Research Unit studies) and the agricultural population figures for the two years. Agricultural population has been estimated at 70 per cent of the total population. The revenue from indirect taxes in 1965-66 has been allocated partly on the basis of 1958-59 per capita tax element figures and partly on the basis of some provisional (unpublished) per capita tax figures for 1963-64. Using the proportions revealed by the allocation of 1958-59 or 1963-64 revenue as between the two sectors, the revenues from indirect taxes in 1965-66 have allocated.

above per month). Per capita tax payment by rural households in that expenditure class at Rs. 1.85 per month was two-fifths lower as compared to urban households in the same group. As per cent of consumer expenditure, tax payment by such rural households was half as much as that by urban households in the same class. Five years later, that is, in 1958-59, also, according to the Ministry of Finance study, while inter-sectoral disparity persisted at all household expenditure levels, rural households in the top expenditure class continued to be comparatively as under-taxed as in 1953-54 absolutely and also relatively to consumer expenditure.

TABLE VII

Tax as per cent of consumer expenditure

Monthly household expenditure (in Rs.)	Taxation Enquiry Commission study (1953-54)		Ministry of Finance Study (1958-59)	
	Rural	*Urban*	*Rural*	*Urban*
1—50	2·2 (0·21)	3·6 (0·45)	2·5 (0·29)	5·8 (0·94)
51—100	2·4 (0·36)	4·5 (0·77)	3·6 (0·60)	7·1 (1·45)
101—150	2·6 (0·54)	5·1 (1·16)	4·1 (0·92)	8·0 (2·09)
151—300	2·8 (0·75)	5·1 (1·54)	4·8 (1·44)	9.0 (2·99)
300—above	4·1 (1·85)	8·2 (4·65)	6·9 (3·84)	13·8 (8·96)

Figures in brackets are tax payments in rupees per capita per month.

Neither the Taxation Enquiry Commission nor the Ministry of Finance could cover the Union and State direct taxes in their study of the incidence of taxes because of the non-availability of data on the distribution of households by income classes. However, if direct taxes like income tax and land revenue were taken into account, the relative under-taxation of the upper rural households would have been much more pronounced than is evident from a study of the incidence of indirect taxes. For, while income tax was borne entirely by urban households in the top expenditure class and income class, land revenue was paid by all agriculturists irrespective

of their expenditure and incomes both in 1953-54 and 1958-59.

Covering both direct and indirect taxes during the period 1950-51 to 1961-62, Ved P. Gandhi made a study of the inter-class inequity in the distribution of tax burden as between agricultural and non-agricultural sectors. He took into account the tax burden on the lower income (below Rs. 3,600 annually) and the upper income (Rs. 3,600 and above annually) groups of the two sectors. His findings, revealing as they are, support the case for additional taxation of agricultural sector, particularly its well-off section :

(1) "The rural households belonging to all brackets of the lower income group paid a lesser percentage of their income taxes than the corresponding group of the urban households. For example, in 1952-53, urban households belonging to Rs. 1,200 to Rs. 1,800 income bracket paid 5 per cent of their income in taxes against that of 3.2 per cent paid by the rural households of the same income bracket. Similarly, in the same year, the population of the income bracket of Rs. 1,800 to Rs. 3,600 in the urban sector paid 5 per cent of its income while the corresponding income bracket of the rural sector paid only 3.6 per cent of its income. If anything this inequity between the lower income groups of the two sectors must have increased since 1952-53 because of the increasing role over time of indirect taxes, which generally fall on the monetised consumption of the urban sector.

(2) "The extent of inter-class inequity between upper income groups of the two sectors is much more serious than that between lower income groups. For example, in 1950-51, the upper income group of the agricultural sector paid about 6.2 per cent of its income in taxes, against 20.5 per cent paid by the upper income group of the non-agricultural sector. The same story holds good for all years since 1950-51. In 1960-61, for example, the upper income group paid only 6.6 per cent of its income in taxes, against 17.8 per cent paid by its counterpart in the non-agricultural sector. Thus the upper income group of the agricultural sector has been enjoying a

great tax advantage over the corresponding group in the non-agricultural sector; this is an indication of serious horizontal inequity.

(3) "Over the period 1950-51 through 1960-61 the upper income group of the agricultural sector carried a marginal tax burden of about 6 per cent to 7 per cent while its counterpart in the non-agricultural sector carries a marginal tax burden of 13 per cent. The equity of marginal tax burden between lower income groups of the two sectors has been much more serious than that between upper income groups. The lower income group of the non-agricultural sector carried a marginal tax burden of about 23 per cent to 24 per cent, against 12 per cent to 13 per cent borne by that group in the agricultural sector."

It is clear that both lower and upper income groups of agricultural sector have borne a significantly lesser average tax burden and marginal tax burden during the years 1950-51 to 1960-61 than have their counterparts in the non-agricultural sector. This indicates horizontal inequity between the two sectors, which should be corrected in the interest of distributive justice by raising the tax burden on higher income groups of the agricultural sector.

TERMS OF TRADE IN FAVOUR OF AGRICULTURAL SECTOR

There is also evidence to show that the agriculturist's capacity to pay taxes must have increased in recent years. As Dr. A.M. Khusro has pointed out that, since inter-sectoral terms of trade have been gradually moving in favour of farmers and against the non-farmers between 1940-50 and again between 1954-61, there is a presumption that the tax paying capacity of the agricultural sector has increased proportionately more than that of the non-agricultural sector. A study of the ratio of foodgrain prices to manufactures (1952-53=100) shows a steady improvement in favour of foodgrain producers. From 91.6 in 1959-60 it dropped to 80.6=100 in 1963-64. Between March 1961 and February 1968, the index of prices (1952-53=100) of agricultural commodities rose from 126 to 213, a rise of 87 points as against a rise of 34 in the case of manufactures, the index of which increased from 130 to 164 in the same period.

During the same period, the index of raw materials registered an increase of 44 points from 159 to 203 an increase which, though smaller than that of the general index of prices of agricultural commodities, was nearly double that of the index of manufactures prices. While this improvement has been taking place in the position of the agricultural sector vis-a-vis the non-agricultural, relative under-taxation of the agricultural sector has been persisting.

NET FLOW OF RESOURCES FROM THE NON-AGRICULTURAL SECTOR

The case for additional agricultural taxation, however, does not rest merely on considerations of inter-sectoral and inter-class equity. An equally strong case for such taxation can be made out on the ground that public investment in agriculture during the plan periods has been very large and it is only fair that agriculture should contribute a reasonable proportion to such investments for its own development. An allocation of Government expenditure to the two sectors can only be rough. However, if on certain assumptions, as have been made by Ved P. Gandhi, Union and State Government expenditures on current account are allocated to the agricultural and non-agricultural sectors, the incidence of Central and state taxation and expenditure on the two sectors indicate a persistent as well as increasing transfer of resources from the non-agricultural to the agricultural sector between 1950-51 and 1962-63.

It will be seen from the Table VIII that whereas, in 1950-51, the agricultural sector paid only Rs. 186 crores in taxes, it received Rs. 286 crores in current expenditure of the Government. The non-agricultural sector, on the other hand, paid Rs. 391 crores in taxes and received only Rs. 286 crores. Thus, in effect, there was an outflow of funds from the non-agricultural to the agricultural sector through the current budget of the Government. The position became still more favourable to the agricultural sector in later years. In 1961-62, for example, the agricultural sector received Rs. 781 crores from the current budget of the Government while it paid only Rs. 413 crores in taxes in the same year. The non-agricultural sector, on the other hand, received Rs. 651 crores, against Rs. 1,095 crores of taxes that it paid to the Government.

TABLE VIII

Tax and expenditure incidence on the agricultural and the non-agricultural sectors

	Total incidence of taxes Union and State		Total incidence of current Union and State expenditure	
	Agricultural sector	Non-Agricultural sector	Agricultural sector	Non-agricultural sector
1950-51	185·52	391·28	286	286
1951-52	199·93	450·58	325	325
1952-53	208·52	427·49	315	321
1953-54	222·12	433·23	330	325
1954-55	234·84	459·99	350	345
1955-56	254·42	461·71	373	349
1956-57	290·67	547·99	443	395
1957-58	344·74	667·99	520	490
1958-59	355·97	713·31	573	496
1959-60	383·64	821·67	606	500
1960-61	398·64	921·60	721	602
1961-62	413·06	1,095·38	781	651
1962-63	502·22	1,325·70	821	686
1963-64	586·76	1,612·80		
1964-65	618·76	1,750·06		

Figures for the years subsequent to 1962-63 are not readily available. However, as there has been no material change since in either the system and trend of taxation or pattern of public outlay, the net flow of resources to the agricultural sector must have been continuing even after 1962-63. The net outflow of funds from the non-agricultural to the agricultural sector *via* the capital budget of the Government was also evident. In the first two years of the Third Plan, for example, the agricultural sector received per annum about Rs. 250 crores of capital expenditure by the Government whereas it contributed only Rs. 75 crores to the capital budget in 1962-63. The transfer of resources, notwithstanding the significance of agriculture for the economy, ought not to be viewed with complete equanimity because it might jeopardise the process of industrialisation in the short run.

DECLINING MARKETING SURPLUS AND LOW PRODUCTIVITY

Additional agricultural taxation is highly desirable if any anti-inflationary incomes policy has to be a reality. It has been claimed that 'prices and marketable surplus tend to move in opposite directions'. Farmers, on what is still mainly a subsistence economy, tend, according to this view, to sell that amount of the output which will give them the amount of money to satisfy their cash requirements and retain the balance of their output for their own consumption. In the context of a rising price level, therefore, it may be desirable to increase the monetary liability on the farmers through additional taxation which will compel them to sell a larger part of their output. This, in consequence, will reverse the declining trend of marketable surplus and the rising trend of prices. The long-term remedy for this tendency to cease to act as a destabilizer of agricultural prices may well be the growth of consumption by the farmer of non-farm commodities; but an increase in taxation could play some part in achieving the same end. The fear that this will be an inflexible element need not necessarily be correct; for taxation can also be made flexible and can vary with the behaviour of prices, just as, at present land revenue remissions and concessions are made to take adverse weather conditions into account.

There is also ground to believe that additional taxation of agriculture might act as a spur to greater effort on the part of the peasant and thus lead to higher agricultural productivity. It is important to recall in this connection that the growth of productivity per worker has lagged behind the growth of investment per worker during the last one decade and more. Various indices are applied to establish this fact. There has been considerable under-utilisation of, for instance, irrigation and fertilizer facilities provided by Government. Inefficient cropping pattern and misutilization of private investible potential are also facts of prevailing slack in the agricultural economy. Hence, there is ground to believe that considerable potential exists for raising agricultural productivity. Government has taken steps to improve the supply of major agricultural inputs and a number of concessions in the supply of credit, etc., have been made available. The price support measures have also been assured.

Thus a considerable financial incentive for improved productivity may be said to have been provided. And it may be that the stick of additional taxation is just what is needed to make the farmers to 'accept the challenge of increased food production in their own interests' without which, as the Ford Foundation Team pointed out, sustained improvement in agricultural productivity may not be achieved. That the expectation of heavier taxation being an incentive for higher productivity is a fanciful idea is demonstrated by the experience of Japan, where land taxation took away about 35 per cent of the industrial produce in the period 1873-1885. Between 1878-85 and 1913-17, land productivity increased by about 80 per cent and labour productivity by 136 per cent. Indeed, as a Japanese writer, who is critical of some aspects of the Meiji land tax, has pointed out, land tax 'may be the most suitable instrument for financing the growth of pre-industrial countries'.

THE MEASURES FOR ADDITIONAL RESOURCES

Given the assumption that during the Fourth Plan period, agricultural income will rise by five per cent annually, the additional income in the five-year period will be Rs. 10,710 crores at 1967-68 prices. Assuming further that the distribution of land holding will not change radically during the period, about three-fifths of the additional agricultural income, *i.e.*, Rs. 6,414 crores, will accrue to farmers having ten or more acres of land as shown in the table below :

TABLE IX

Increase in agricultural income

(assuming five per cent annual increase at 1967-68 prices)

(Rs. in crores)

	Agricultural income*	Increase over 1968-69	Share of well-off farmers† in (2)
1968-69	13,330	—	—
1969-70	14,000	670	400
1970-71	14,700	1,370	820
1971-72	15,435	2,105	1,260
1972-73	16,207	2,377	1,724
1973-74	17,017	3,687	2,210
		10,709	6,414

*Estimated.

†Farmers with ten acres or more of land.

Against this, if the target of additional mobilisation of resources by the State during the Fourth Plan period is fixed at Rs. 1,500 crores, funds amounting to Rs. 1,000 crores can be raised additionally in the agricultural sector through a combination of borrowing, taxation and certain non-tax measures and almost exclusively from its well-off section. The specific measures which can be adopted for mobilising resources of this order, without inflicting any hardship, are discussed below.

BORROWING

The well-to-do agriculturist has been saving a part of his income. But he has not been a lender to the same extent, having a strong preference for assets like cash and precious metals both of which he can keep with himself, the former being perfectly liquid and the latter easily marketable and currently a hedge against inflation. The All India Rural Household Survey made by the National Council of Applied Economic Research shows that about Rs. 105 crores or 50 per cent of the net increase in the financial assets of rural households in 1962 was in the form of currency (Rs. 65 crores or 30 per cent) and gold and silver (Rs. 40 crores or 20 per cent). The survey, further, estimates the marginal propensity to save (proportion of additional saving to additional income) of rural households at about 17 per cent including holding of currency. On that basis, saving out of the additional agricultural income during Fourth Plan period would amount to Rs. 1,820 crores, additional income being estimated at Rs. 10,710 crores during the period. If this additional saving involves the same proportionate acquisition of currency and gold and silver by the agricultural sector as in 1962, the sector will add about Rs. 400 crores of these assets to their wealth in the Fourth Plan period. This will be in addition to what they will add during the Fourth Plan period on the basis of their pre-Fourth Plan period annual income; and that addition may be taken at around Rs. 525 crores on the assumption that they will only maintain the absolute order of acquisition of these assets revealed by the survey referred to above. Thus the total net addition to the financial asset-holding of the agricultural sector during the Fourth Plan period can be placed at about Rs. 925 crores.

The calculations made here are, no doubt, mechanical. For, they do not take into account the change in the pattern of acquisition of financial assets which, over time, might have occurred with the rise in income and wealth. It can perhaps be maintained with reason that the order of acquisition of these assets will be less than has been assumed here. However, their purpose is served if it has become evident that only if the agriculturist can be induced to lend, instead of increasing his hoard of currency and gold, quite a sizable amount of funds can be raised by means of borrowing. For there are, besides, hoards of currency and gold and silver accumulated by the agricultural sector in the past to tap. Therefore, the target of borrowing from the agricultural sector can be put at Rs. 60 crores a year or Rs. 300 crores in the entire Fourth Plan period. The State-wise break-up of the target is given in Appendix I.

The crucial consideration is the provision of sufficient inducement to land. A very high rate of interest as an inducement will be undesirable for a number of reasons. It will lead to a competitive rise in interest rates throughout the economy. It will increase for Government the cost of servicing its debt. Above all, it will, by attracting non-agricultural savings, defeat the very objective of raising additional resources from the agricultural sector. However, a high rate of interest will be unnecessary and the objective of mobilising savings in the agricultural sector can be achieved if the agriculturist can be convinced that, if he will lend, he will himself gain in addition to the market rate of interest on his loan. A plan for financing agro-based industries with resources raised from the agricultural sector through the sale of debentures and supplemented by the financial participation of Government and financial institutions can convince the agriculturist and eventually induce him to lend his savings. For such industries will not only mean employment in the rural sector and remove the pressure on land but also provide ready and close market for the sale of agricultural products and purchase of agricultural inputs and also necessary repairing services and consumer goods at fair prices. And taken together these benefits will directly or indirectly tend to raise the agriculturists' income and thus provide an adequate inducement to them to take up the agro-industrial debentures. If these

benefits constitute, in effect, the principal attraction of the debentures, they will also effectively isolate the debentures from changes in market interest rates. Since, further, such of the urban investors as have an interest in agriculture will not be able to avail of these benefits of investment in agro-based industries, they will have no incentive to provide loans for such industries, even if a slightly higher interest rate as compared to industrial and financial debentures is paid on them.

The Cooperative Central Land Mortgage Banks have been selling rural debentures as distinguished from the ordinary debentures which are meant for urban sectors; and they have become popular in rural areas in recent years when the funds raised have been utilised for setting up processing industries in the country side. The agro-industrial debentures, it can be expected, will also be popular in rural areas. For they will directly benefit each agriculturist one way or the other in and around the locality where an agro-industry will be set up. And the benefits of such industries will be immediately many-sided-employment opportunities and ready market for sales as well as purchase of articles in which an agriculturist is interested as a producer as well as a consumer.

TABLE X

Rural Debentures

(Rs. in lakhs)

Year	Amount floated	Amount subscribed	
		Individuals	Reserve Bank of India
1957-58	75.00	34.09	26.88
1958-59	90.00	38.07	42.70
1959-60	71.47	33.90	37.57
1960-61	155.09	59.06	67.48
1961-62	225.00	85.00	96.76
1962-63	157.00	61.62	70.42
1963-64	184.00	74.00*	84.59
1964-65	323.00	114.00*	130.00
1965-66	433.00	149.00*	170.00
1966-67	293.00	80.00*	92.00

*Provisional figures.

Even so, interest in any case will have to be paid on them at a rate not unattractive considering the yields of industrial and financial debentures and the agriculturist's preference for liquid and near-liquid assets—the latter, in the form of precious metals, being also perfectly marketable. Since agro-industrial debentures will have to compete with cash in the agriculturist's asset portfolio, they will have to be liquid. Further, as they will carry a rate of interest, their liquidity will inevitably be related to the stability of market rates of interest; and the maintenance of stability will impose a greater responsibility on the monetary authorities.

The marketability of agro-industrial debentures will depend on their popularity and their popularity, in turn, will depend on: (*i*) the agriculturists' appreciation of the benefits of the agro-industries together with the interest rate available on them, (*ii*) the security which the financial participation of the Government and the financial institutions will provide, (*iii*) the correspondence between supply of and the demand for the debentures by their maturity pattern, on the one hand, and their denomination pattern, on the other, (*iv*) their negotiability, and (*v*) the soundness of the conception and the efficiency in the management of the agro-based industrial units.

Given an intensive drive backed by vigorous publicity and suggestions from local leadership, the benefits of agro-industry and the advantages of Government financial participation can be brought home to the agriculturists. As for the maturity and denomination patterns necessary to make the agro-industrial debentures marketable, some intensive study of the pattern of time horizon, asset preference and savings by the upper income groups in the agricultural sector will have to be undertaken. It is certain, however, that the agro-industrial debentures will have to be sold in different maturities and denominations in order to make a wide appeal.

If agro-industrial debentures can be issued primarily on the basis of the benefits which agro-based industries are expected to confer exclusively on the agriculturists and are, therefore, not taken up by non-agriculturists, they can be issued as bearer bonds and, in effect, made negotiable. Negotiability is a necessary condition to make them marketable and thereby increase their

popularity. But given negotiability, the degree of their marketability, that is, their acceptability in the agricultural sector will depend as much on the stability of their value in the market as on the stability of prices in general. For, as financial assets they will have to compete with, besides cash, precious metals which are not only perfectly marketable but also provided a hedge against inflation. The monetary authorities, therefore, will have to maintain stability in interest-rates and price-level, if agro-industrial debentures are to be an effective means of mobilising resources from the agricultural sector.

Agro-based industries can be of very many types and the capital investment necessary for them ranges from over Rs. 1 lakh to Rs. 250 lakhs if sugar factories are included. To fulfil the basic condition for the success of agro-industrial debentures only such industrial projects should be selected as would not require a large amount of capital but at the same time would be profitable in themselves and beneficial to the agriculturists of or near the area in which they are set up. There should be, in short, a bias for labour intensive industries and processes. For, besides economising in capital, they will be more employment-creating. If on an average, the agro-based industries chosen for being set up require a capital investment of Rs. 3 lakhs, not more than 4,000 such industrial units can be set up in a year, if agro-industrial debentures worth Rs. 60 crores a year are actually sold and the State Governments and financial institutions invest another Rs. 60 crores. At this rate, in five years, 20,000 agro-based industrial units can be set up, and this will mean three to four industrial units for a group of six village units or roughly 60,000 heads in the Fourth Plan period—not a discouraging beginning on a new line.

NON-TAX MEASURES

(1) **Collection of arrears** : The total arrears of tax and non-tax revenues and loans and advances as at the end of 1966-69 are estimated at Rs. 376[11] crores (*vide* Appendix II). Of this, Rs. 245 crores or about 70 per cent is attributable to five States, *viz.*, Bihar, Assam, Kerala, West Bengal, Madhya Pradesh, Andhra Pradesh and Uttar Pradesh. The main reason for the

[11]This figure, however, does not give a complete idea of arrears because some States have not supplied full information.

mounting up of the arrears to such a high figure has been bad harvests during the last two years. However, in view of the improved agricultural situation it should now be possible for the States to undertake a vigorous drive for collecting the arrears. It is suggested that the States should endeavour to recover a total amount of about Rs. 21 crores per annum or Rs. 105 crores during the Fourth Plan period as indicated in Annexure III. Even with the materialisation of this, there would be left outstanding arrears of Rs. 270 crores at the close of the Fourth Plan period. It need hardly be mentioned that in order to achieve the proposed targets the States will have to make a serious effort. Not only this, care will have to be taken to see that no further addition is made to the outstandings.

(2) **Withdrawal of subsidies :** The State Governments have been giving various types of subsidies for agricultural development, and these involve financial costs to the state exchequers. In view of the fact that the agriculturists especially the larger ones, are now in a position to meet the cost of agricultural inputs and adopt improved practices from out of their own resources, it is felt that the subsidies can be withdrawn in a large number of cases. Some of the subsidies have the objective of reducing the cost of certain essential but costly inputs till their popularity is established. In such cases also wherever the subsidised inputs have gained popularity, it should not be difficult to eliminate the subsidies. It may, however, be necessary to continue subsidies from selected areas and for small farmers.

Although some of the States have taken action to abolish or reduce some of the subsidies, still there are quite a many of them which need to be curtailed. For example, subsidies in respect of pesticides, implements and pumpsets, which have become quite popular, should be withdrawn immediately. There are others which can be tapered off with a view to abolishing them altogether as quickly as possible. In the absence of the availability of specific data, it is not possible to arrive at any precise figure, but the scrapping of subsidies on a selective basis would mean a saving of resources to the State Governments.

(3) **Increase in matching contribution to loans and advances:** As in the case of subsidies, there is considerable scope for

effecting savings by reducing the Government's contribution in respect of loans and advances given by the States to third parties for various purposes under agricultural development schemes. For example, at present, the purchaser of a tractor or a diesel pump initially pays only 50 per cent of the cost and the remaining 50 per cent is contributed by the Government in the form of long-term loans repayable over a period of 15 years. This type of contribution by the Government can be easily done away within the case of well-to-do farmers. In the case of other farmers also, it should generally not be difficult to reduce the Government's contribution and to increase the farmer's by 50 per cent or so. Again, there are certain schemes such as sinking of tube wells and purchase of bullocks, where the agriculturists get the full cost by way of the medium-term loans. In such cases, the farmers should be gradually made to meet more and more of the cost so as to reduce the loan burden of the Government. In deciding these, however, the stage of development of a region, the special needs of backward areas and the requirements of small farmers, will have to be kept in view.

In the absence of full information regarding matching contributions, it is not possible to indicate a precise figure for this item also. But saving due to this measure is expected to be of a sizable order.

(4) **Irrigation rates:** Irrigation projects are, at present, not giving adequate financial returns. According to the latest estimates, the loss on commercial irrigation works in 1968-69 is put at about Rs. 60 crores. This is exclusive of the loss on irrigation works under the multi-purpose river valley projects estimated at Rs. 16 crores. However, except in scarcity areas, irrigation schemes should not incur loss if with the increase in the value of crops produced as a result of irrigation, the rates are commensurately increased. The Nijalingappa Committee has recommended, *inter alia*, that irrigation rates should be levied suitably at 25 to 40 per cent of the additional net benefit to the farmer from the irrigated crops where such benefit can be estimated; else they can be levied at 5 to 12 per cent of the gross income from the irrigated crop. The Committee has further suggested that a compulsory surcharge, sufficient to cover at least the maintenance and operational charges of

irrigation works, should be made applicable to the entire area where irrigation facilities are provided irrespective of whether water is taken by a cultivator or not. If by implementing in stages the recommendations of the Nijalingappa Committee and increasing utilisation of irrigation facilities, where it is low, the current loss of Rs. 76 crores a year is brought down to around Rs. 10 crores, by the end of the Fourth Plan period, additional revenue amounting to Rs. 200 crores can be raised during the period. The Statewise break-up thereof is given in Appendix III.

TAXATION

At present, agricultural income tax is being levied by nine States, *viz.*, Assam, Bihar, Kerala, Madras, Mysore, Maharashtra, Orissa, West Bengal and Jammu & Kashmir. Uttar Pradesh collects it in the form of a tax on large holdings. Rajasthan abolished agricultural income tax in 1960; and like Punjab, it now levies a surcharge on land revenue. The total collection in all the States taken together comes to about Rs. 11 crores. Out of this, Rs. 10 crores is accounted for by five States, *viz.*, Assam, Kerala, Madras, Mysore and West Bengal. Of this also, 85 per cent is attributable to plantation. The revenue from the tax on non-plantation agricultural income is, indeed, nominal.

In Jammu & Kashmir and Orissa, the collection is insignificant from the revenue point of view. In Bihar and Orissa, it has declined to less than half of what it was in 1960-61 and in West Bengal from Rs. 107 lakhs in 1960-61 to Rs. 26 lakhs in 1967-68. Moreover, some States allow special exemptions. For example, in Maharashtra the tax has been designed mainly for large sugarcane farms and for that also the exemption limit has been pitched as high as Rs. 35,000 as against Rs. 3,000 recommended by the Taxation Enquiry Commission. In Mysore, agricultural incomes derived from land under commercial crops only are taxable. In Jammu & Kashmir, incomes derived from orchards, Maliari land or from cultivation of fruit plants only fall within the purview of the tax. Consequently, the growth in revenue from this tax has not been at all commensurate with the increased income generated in the agricultural sector. The total collections which amounted to Rs. 9.6 crores in 1960 rose to only Rs. 11 crores by 1967-68, that is, an increase of

Rs. 140 lakhs or nearly 15 per cent in seven years, as against an increase of 12 per cent per annum on an average in agricultural income in recent years. More significantly, the revenue from the tax in 1967-68, if it is spread over the total income of farmers having ten acres or more of land in a year, works out to a mere 0.1 per cent of such income. This shows, in other words, the negligible burden which the current revenue from agricultural income tax will impose on the well-off agriculturist if it were-raised by all the States through a uniform rate schedule adjusted to it. As a corollary it follows that agricultural income tax has very large revenue potentialities.

The Taxation Enquiry Commission, 1953-54 had recommended that all States should levy agricultural income tax for attaining greater equity in their tax system and elasticity in their tax revenues. The ultimate aim of the Commission was, however, the merging of agricultural income and non-agricultural income and levy of one income tax. The assimilation of the two taxes will, undoubtedly, effect horizontal as well as vertical equity between agricultural and non-agricultural incomes and income earners. It will also effect as compared to the present, greater productivity as well as elasticity of the combined revenue of the two taxes. For, if agricultural and non-agricultural incomes are combined for tax purposes, a number of income earners, now enjoying tax exemption, will be brought into the tax net, while others will, because of the combination of the two categories of incomes be liable to high rates of tax. The adding up of the two types of incomes will also close a loophole for avoiding income tax. Thus, from the point of view of both fiscal equity and mobilisation of agricultural surpluses, the reform by way of merger of agricultural income tax with the central income tax is urgently called for.

No doubt, in the initial stages of the enforcement of the tax there will be some difficulties, relating mainly to the determination of agricultural income, in implementing the proposed merger; but ways can be found to surmount them. For instance, in the U.S.A. option is given to farmers to elect the accrual method of accounting or the cash method or the crop method for the computation of taxable income. This relaxation is based upon the consideration that few individual farmers have the training

or facilities to maintain books and records adequate to support any accrual system and that even in respect of larger farmer-organisations, book-keeping personnel are not readily available in farm areas. In U.K., the owner or occupant of farm lands is assessed on the basis of his presumptive incomes as reduced by the statutory repair allowance equal to one-eighth thereof. In Mexico, taxpayers with gross annual income of more than Pesos 10,000 but less than Pesos 2,00,000 are taxed on the basis of the gross income while those with gross annual income of Pesos 2,00,000 or more are taxed on net income. In Brazil, two methods are permissible for taxation of agricultural income. If the taxpayer keeps reliable books and records showing his gross income and expenses, he may elect to be taxed on net income. The law does not prescribe any particular books or methods of book-keeping for these taxpayers as it does for other entities. Any informal records which clearly disclose income and expenses are acceptable to the fiscal authorities. If the taxpayer keeps no books or maintains books not acceptable to fiscal authorities, the law substitutes an amount of five per cent of the value of the property as the net income on which tax is computed. The property included are land and pastures, buildings and other improvements, equipment, agricultural machines, permanent crops, work animals and animals held for income. Where the value of all property cannot be exactly determined, the fair market value of the land plus 10 per cent to cover all other items is taken as the basis for computing taxable net income. In Switzerland, schedules of presumptive assessments are set up over ten years and taxes are levied on the basis of these assessments. However, the farmer has the right to a revised assessment based on actual income if he can show that his actual income is less than two-thirds of that presumed, and Government takes the right to tax actual income if it is one-third or more above the presumed amount. This is done presumably to discharge wholesale claims for tax reviews. Procedures similar to these would make it unnecessary to rely on book-keeping and might in fact encourage large farmers to keep books if they feel that they are over-assessed. A similar system can be tried in this country. Uganda has also a faculty tax for which income from agriculture is assessed on a presumptive basis.

Although the final objective has to be the merger of the two taxes, yet, because its actual implementation may take time and the need for raising additional resources is an urgent one, the following steps are suggested for immediate implementation.

(1) States of Andhra Pradesh, Gujarat, Haryana, Punjab, Rajasthan and Nagaland, which at present do not have agricultural income tax, should impose it forthwith. In U.P. also, the tax on large land holdings does not appear to be a proper substitute for this tax and should be replaced by agricultural income tax.

(2) States which are having this tax at present should amend their enactments so as to increase their coverage both by type of crops and size of income whenever possible. In fact, all States should fix the exemption limit at Rs. 4,000 for individuals, and all exemptions in respect of crops should be withdrawn.

(3) The tax should be levied on presumptive net income from farming based on size of holdings, crops grown, inputs used, etc., where assessments based on return of income and expenses are not possible. Alternatively, agricultural income tax may be assessed at five per cent of the market value of capital assets, land, buildings, equipments, irrigation work, etc., used in agriculture, where details of income and expenses are not available.

(4) The rate-schedule of the tax should be revised upward so as to bring it closer to the rate-schedule of central income tax.

(5) The machinery for assessment and collection of agricultural income tax should be strengthened and its administration streamlined so as to effectively assess the tax and check evasion.

The additional revenue, which a thorough implementation of the above suggestions may yield, is estimated at around Rs. 138 crores a year on the basis of 1967-68 income from agriculture (less the wage share of agricultural labourers) and 1961-62 distribution of operational holdings by households

(as indicated by the National Sample Survey). The method of estimation of the revenue is indicated in Appendix IV.

Since the suggestions made above cannot be fully implemented immediately by all the States, but remembering on the other hand, that nine States where the tax is in operation, need only tighten administration, the additional yield of the tax in the first year of the Fourth Plan has been taken at Rs. 60 crores. With progressive implementation of the suggestions and agricultural income rising by 5 per cent annually, the additional revenue potential of the tax will go up to about Rs. 135 crores by the final year of the Fourth Plan. However, since some allowance has to be made for tax incentives in the interest of higher productivity and larger savings in the agricultural sector, the additional revenue from the tax, it is assumed, will rise by Rs. 10 crores a year to Rs. 100 crores by the closing year of the Fourth Plan and amount to Rs. 400 crores in five years.

Administratively, agricultural income tax will not, on the whole compare unfavourably with central income tax, though agricultural income shows less concentration at higher income levels than taxpaying non-agricultural income. For assessment of agricultural income will be relatively easy since in a locality soil characteristics and cropping pattern do not vary much from holding to holding. A few regular assessments can set the standards to be broadly applied to all the assessees in the area. If, further, local knowledge and experience are made use of through panchayats, assessments will become easy and the standards once set up can be applied year after year, in the absence of a basic change, by taking into account variation in rainfall and weather conditions. In the case of non-agricultural income, on the other hand, each return has its own peculiarities and, therefore, needs to be scrutinised with care, specially if returns relate to business income or to large incomes derived from different sources.

CONCLUSION

It has been said that by borrowing from the agricultural sector, the State Governments can raise funds amounting to Rs. 300 crores in five years. By levelling up irrigation rates as per cent of gross income from irrigated crops Rs. 200 crores can be

raised from irrigation projects during the same period. Another Rs. 100 crores can be provided for by collecting arrears of revenue and selectively withdrawing subsidies and matching grants where they are not called for. If agricultural income tax is introduced in States where it is not in force and in all States if the suggestions already made for its development are implemented, additional resources from the agricultural sector will be not less than Rs. 1,000 crores in the aggregate, additional revenue from agricultural income tax in five years being taken at only Rs. 400 crores, as against its much larger revenue potential. Thus, by suitable measures and combination of taxes, additional resources amounting to Rs. 1,000 crores can be mobilised from the agricultural sector during the Fourth Plan period. The measure-wise break-up of additional resources from the agricultural sector is indicated below:

TABLE XII

Additional resources from the agricultural sector during the fourth plan period

(Rs. in crores)

1. Agro-industrial debentures	300
2. Collection of arrears of taxes, etc., and withdrawal of subsidies and matching grants	100
3. Irrigation rates	200
4. Agricultural Income Tax	400
Total	1000

As the sale of agro-industrial debentures is expected to draw into the exchequer savings which would otherwise be hoarded, it will involve no burden on the agriculturist; further it will be well within their estimated additional hoards of currency and precious metals during the Fourth Plan period. Irrigation rates, if introduced to cover the current and capital cost of irrigation works, are a payment for a service which by raising productivity of land increases the agriculturist's income. They cannot, therefore, be said to impose a burden on agriculture. So, strictly speaking, only agricultural income tax will impose a money burden of Rs. 400 crores if the additional resources are taken at Rs. 1,000 crores. Related to the estimated additional

income of the well-off agriculturists in the Fourth Plan period, the additional tax burden will be 6.2 per cent. Spread over the estimated annual total income of the well-off agriculturists during the Fourth Plan period, annual additional tax burden will amount to 0.86 per cent and annual additional resources to be raised will work out to 2·2 per cent.

(1)	Additional income of the well-to-do agriculturists during the Fourth Plan period.	Rs. 6,414 crores
(2)	Annual average of total income of well-to-do agriculturists in the Fourth Plan period.	Rs. 9,283 crores
(3)	Additional tax burden (Rs. 400 crores) as percentage of (1)	6.2 per cent
(4)	Annual additional tax burden as percentage of (2)	0.86 per cent
(5)	Annual additional resources as percentage of (2)	2.2 per cent

A consolidated table showing the state-wise and measure-wise break-up of additional resources (Rs. 1,000 crores) from the agricultural sector during the Fourth Plan period is given in Annexure V. The additional resources indicated here, it may be noted, are exclusive of the additional burden of state taxes (like sales taxes, excise duties, etc.), which the agricultural sector will have to bear along with the non-agricultural sector during the Fourth Plan period.

Appenidx I

State-wise sale of rural debentures during the Fourth Plan period

(Rs. in crores)

S. No.	*Name of State*	*Estimated sale of debentures*
1.	Andhra Pradesh	25
2.	Assam	7
3.	Bihar	12
4.	Gujarat	27
5.	Haryana	15
6.	Jammu & Kashmir	—
7.	Kerala	21
8.	Madhya Pradesh	19
9.	Madras	28
10.	Maharashtra	24
11.	Mysore	21
12.	Orissa	10
13.	Punjab	37
14.	Rajasthan	7
15.	Uttar Pradesh	26
16.	West Bengal	21
	Total	300

Appendix II

Fourth Plan targets of collection of arrears of tax and non-tax revenues and overdue loans and advances

(Rs. in crores)

S. No.	States	Estimated arrear of tax and non-tax revenue and overdue loans and advances as at the end of March, 1969	Collections suggested over Fourth Plan period	
			Per annum	Over five years
1.	Andhra Pradesh	28.87*	1.0	5.0
2.	Assam	38.43*	0.8	4.0
3.	Bihar	71.1	3.0	15.0
4.	Gujarat	10.5	1.0	5.0
5.	Haryana	3.9	0.5	2.5
6.	Jammu & Kashmir	14.15*	0.8	4.0
7.	Kerala	39.17*	1.0	5.0
8.	Madhya Pradesh	29.9	1.8	9.0
9.	Madras	13.79	1.0	5.0
10.	Maharashtra	16.35*	2.8	14.0
11.	Mysore	19.8	1.0	5.0
12.	Nagaland	—	—	—
13.	Orissa	15.4	1.0	5.0
14.	Punjab	3.57*	0.7	3.5
15.	Rajasthan	8.0	1.0	5.0
16.	Uttar Pradesh	24.33*	1.8	9.0
17.	West Bengal	38.3	1.8	9.0
	Total	375.54	21.0	105.0

*Latest information obtained from States in connection with the estimates of resources for the Fourth Plan.

Appendix III

Additional Revenue from Irrigation rates during the Fourth Plan Period

(Rs. in crores)

S. No.	States	*Net receipt from irrigation projects—1968-69*			*Collection target*
		Commercial Irrigation	*Multi-purpose projects*	*Total*	
1.	Andhra Pradesh	– 11.10	– 8.45	– 19.55	42
2.	Assam*	—	—	—	..
3.	Bihar	– 1.12	– 2.67	– 3.79	15
4.	Gujarat	– 4.04	—	– 4.04	10
5.	Haryana	– 1.39	– 1.19	– 2.58	6
6.	Jammu & Kashmir	– 0.49	—	– 0.49	1
7.	Kerala	– 1.32	—	– 1.32	3
8.	Madhya Pradesh	†	†	†	15
9.	Madras	– 5.02	—	– 5.02	11
10.	Maharashtra	– 7.25	+ 2.00	– 5.25	12
11.	Mysore	– 6.04	—	– 6.94	17
12.	Orissa	– 4.17	– 3.86	– 8.03	17
13.	Punjab	– 2.68	+ .08	– 1.83	4
14.	Rajasthan	– 2.83	– 2.63	– 5.46	12
15.	Uttar Pradesh	– 11.28	—	– 11.28	25
16.	West Bengal	†	†	†	10
	Total	– 59.63	– 15.95	– 75.58	200

*Irrigation rate is not presently levied in Assam.
†Relevant data are not available.

Appendix IV

Method of estimation of revenue from Agricultural Income Tax

1964-65 is the latest year in respect of which state-wise distribution of agricultural income, inclusive of animal husbandry, at current prices is available on a comparable basis. The percentage share of each State in all-India agricultural income in 1964-65 has been used to obtain the state-wise distribution of agricultural income, exclusive of animal husbandry, at current prices in 1967-68. The implicit assumptions in this derivation are, while obvious, inescapable because of limitation of data. The 'derived' agricultural income of each State has then been divided by the area of operational land therein (as indicated in the Report on the 16th Round National Sample Survey relating to 1961-62*) to obtain the per acre income in different States in 1967-68.

For calculating the income accruing to the households in an operational-holding-size-class of a State, the midpoint of the holding-size-class has been taken; and the product of the midpoint of a holding size-class and the per acre income in the State has been taken as the average household income of that holding-size-class in that State. Agricultural income tax payable on the average household income in each holding-size-class in different States has been worked out by applying central income tax rates to the average household income. This involves the assumption, not always correct, that each household has only one earner†. Since state-wise allowance cannot be made for the two-or-more-earner households on the basis of available studies, this assumption has been adhered to at this stage of the estimation process.

The tax payable on the average household income of each holding-size-class in a State has been multiplied by the number of households therein, as indicated in the Report on the 16th Round National Sample Survey, to get the total tax payable

*1961-62 is the latest year for which such data are available.

†A married earner with more than one child.

by households in each holding-size-class in a State. By totalling up the tax payable by the households in different holding-size classes in each State, the likely yield of agricultural income tax in different States has been arrived at. Finally, the state-wise estimated revenue figures have been aggregated to get the all-India estimate of the likely yield of agricultural income tax. This works out to Rs. 257 crores a year assuming agricultural income at the 1967-68 level and one-earner households.

To allow for the existence of two-or-more-earner households, the results of an estimate of revenue from agricultural income tax on the basis of data available in the All-India Rural Household Survey (relating to 1961-62) by the National Council of Applied Economic Research have been made use of. The NCAER Study estimated the number of rural households by number of earners in different income brackets. Assuming the same distribution in proportionate terms of farmer households by number of earners in different income brackets, the revenue from agricultural income tax was estimated at Rs. 115 crores on the basis of 1967-68 agricultural income and central income-tax rate schedule. The method of estimation is given in the supplement to this annexure. The revenue from the tax was estimated also by assuming only one earner in each farmer household and the estimate came to Rs. 214 crores. The percentage difference between these two estimates on the basis of NCAER data has been used to deflate the State-wise estimates arrived above at para 3 on the basis of derived State-wise agricultural income and assuming one-earner households and thus allowing for two-or-more-earner households. The *adjusted all-India estimate of revenue from the tax works out to Rs. 138 crores.*

Supplement to Appendix IV

Estimation of Revenue from Agricultural Income Tax

All India Rural Household Survey by the National Council of Applied Economic Research has estimated:

(1) agricultural wage income,

(2) agricultural non-wage income accruing to rural households in 1962.

It also estimated the agricultural income which accrued to self-employed farmer households in that year and the proportion of total income which accrued to self-employed farmer households in different income-brackets.

On the basis of relevant proportions worked out from these estimates, the total non-wage agricultural income of self-employed farmer households in 1967-68 has been estimated, taking 1967-68 income from the agricultural sector at Rs. 12,675 crores. The total estimated non-wage agricultural income of these households has been allocated to different income-brackets in proportion to their shares in such income as revealed by the NCAER study. The inescapable assumption here is that the incomes of the different NCAER household groups by income brackets increased at the same rate between 1962 and 1967-68.

The NCAER study also estimated the number of rural households by number of earners in different income-brackets. For self-employed farmer households the same proportions have been assumed. The average income of self-employed farmer households in different income-brackets in 1967-68 has been arrived at by dividing the share of each income-bracket in the total non-wage agricultural income of such households by the number of such households therein as given in the NCAER survey. Owing to the large increase in income since 1962-63, the NCAER household groups, it may be noted, move up the income scale.

The estimate of revenue from agricultural income tax in 1967-68 has been made by applying the Central income tax rates to the average household income in different income brackets. Households with one earner present problem. As for those with two earners, it has been assumed that on an average, 75 per cent of the household earning was contributed by one earner and the balance by the second. As regards households of three or more earners, the assumption has been that one earner contributed 60 per cent of the total household income.* The NCAER study points out in its second volume that about 84 per cent of the incomes of self-employed farmer households were derived from non-wage agricultural income. If this is taken into account, the contribution of the principal (self-employed farmer) earner in the two-earner households to their total income works out to 63 per cent and that in the three or more earner households to 50 per cent. The assumption regarding the contribution of the principal earners in the two or three or more earner households, therefore, does not seem to be unrealistic.

The estimate of revenue from agricultural income tax on the basis of 1967-68 agricultural income and NCAER data used for this are presented in the statement below :

STATEMENT I

NCAER All India Rural Household Survey

Income Bracket	Number of households in '000	Income in 1962-63 Rs. crores	Number of households by number of earners in '000		
			Upto one	Upto two	Three or more
Upto Rs. 3,600	30,490	4,069·81	—	—	—
Rs. 3,601-4,800	1,244	510·69	446	357	441
Rs. 4,801-7,200	670	384·46	189·6	191·0	289·4
Above Rs. 7,200	468	589·26	132·4	133·4	202·2
Total	32872	5554·22			

*These assumptions are based on the NCAER finding that in the case of more than 90 per cent households the maximum income is contributed by a single member who is designated as the chief earner of the household.

Statement II

Estimate of Revenue from Agricultural Income Tax

NCAER household	Income in 1967-68 (Rs. crores)	Average income in 1967-68 (in Rs.) per household	Average Tax payable by households by number of earners			Tax Revenue (Rs. in crores)
			Upto 1	Upto 2	Three or more	
30,490	7,092	2,326	Nil	Nil	Nil	Nil
1,244	890	7,154	248	52	Nil	12·9
670	668	9,970	558	248	119	18·8
468	1,026	21,923	3,120	1,547	1,081	83·8
	9,676					115·5

Note : If only one earner is assumed for each household the revenue from tax will amount to Rs. 214 crores.

Appendix V

State-wise and measure-wise break-up of additional resources to be raised from the agricultural sector during the fourth Plan Period

(Rs. in crores)

State	*Rural debenture*	*Tax and non-tax arrears*	*Irrigation rates*	*Agricultural income tax*	*Total*
1	2	3	4	5	6
1. Andhra Pradesh	25	5	42	38	110
2. Assam	7	4	*	10	21
3. Bihar	12	14	15	15	56
4. Gujarat	27	5	10	35	77
5. Haryana	15	2	6	20	43
6. Jammu & Kashmir	—	4	1	1	6
7. Kerala	21	5	3	28	57
8. Madhya Pradesh	19	8	15	32	74
9. Madras	28	5	11	34	78
10. Maharashtra	24	13	12	41	90
11. Mysore	21	5	17	21	64
12. Orissa	10	5	17	20	52
13. Punjab	37	3	4	30	74
14. Rajasthan	7	5	12	9	33
15. Uttar Pradesh	26	9	25	37	97
16. West Bengal	21	8	10	29	68
Total	300	100	200	400	1000

*Irrigation rate is not presently levied in Assam.

B. EXTRACT FROM CHAPTER I OF THE TAXATION ENQUIRY COMMITTEE REPORT OF THE GOVERNMENT OF KERALA

Indian Union comprises States and regions of extreme diversities in size, density of population, historical and cultural heritage, natural endowments as well as social and economic development. Regional disparities in the pre-British period were mainly attributable to historical and natural factors. But the commercial and industrial development that characterised the British period (especially during the last hundred years) aggravated the lopsided development of the different regions. The layout of the railways limited the process of modernisation to the leading ports and other transport breaking points. The locational advantages indicated by the framework of transport and communication snow-balled the process of development in a few urban areas which attracted capital, raw materials and labour from elsewhere. The network of financial institutions helped forward the mobilisation of surplus resources from all over the country and channelled them into areas of intense economic activity.

Some of the regions possessing immense natural advantages had to remain backward in the face of strong locational pulls exerted by these man-made factors. Even a fair degree of activity of mining, plantations and processing could not elevate many of them to be ranked as developed regions. The existence of princely states with their predominantly feudal socio-economic fabric and in most cases with backward standards of administration added another dimension to the problems of regional disparities. Barring a few, most of these princely states constituted some of the most backward regions of the Indian Union. A measure of such disparity is the wide difference in the per capita income of the different states. The anxiety of the poorer states to overcome their backwardness in development can easily be understood. But the mechanism for mobilisation, allocation and transfer of resources has not been quite conducive to a progressive reduction of regional disparities.

As in most other federations there is a growing divergence between the responsibilities arising from the original distribution of powers and fiscal capacity between the Union and State Governments in India especially under the weight of successive Plans for economic and social development. As it has come to be, the Centre is concerned with the most generalised features of the national frame (such as the creation and maintenance of the credit and monetary system, railways and ports, as well as the facilities for national economic planning) and with highly concentrated action at a few strategic points (such as the regulation and development of large-scale industries, exploitation of mineral resources, state trading, regulation of foreign trade, etc.). On the other hand, the States are concerned with acting on the total life of the people transmitting the forces impelling economic development to all areas and units as well as with concretising the fruits of development to all the individuals within their territories. Infrastructure investment such as irrigation, power and regional and local roads as well as the outlays on human resources through the development of educational and health facilities are the responsibilities of the States. The generation of income and employment largely depends on the extent to which the State Governments could promote the primary industries such as agriculture, forests, fisheries, mining and the secondary activities in the small and medium industries apart from conserving traditional handicrafts.

In fulfilling these devolved responsibilities the States have become increasingly dependent on the Centre for their current as well as capital resources. Of the total expenditure of States (Plan and non-Plan) excluding the discharge of repayment of debt, the resources from the Centre have increased from 42 per cent in the First Plan to 49 per cent and 52 per cent respectively in the Second and Third Plans. More than 53 per cent of the total resources so transferred consist of loans. Of the balance more than half is attributable to grants-in-aid (revenue and capital) the remaining being States' share of divisible taxes. The relative share of statutory grants has suffered a striking decline over the Plans and during the first fifteen years of planning, discretionary grants were more than twice as large as statutory grants. The same trend has continued since then. Such a dependence is the natural consequence of the enormous command

enjoyed by the Centre over relatively larger and larger revenue resources mobilised through the fiscal system besides those available from banks, insurance, foreign trade and assistance, postal deposits and other sources of non-tax revenue. On the capital side, the massive indebtedness of the States has led to a kind of creditor-debtor relations between partners breeding a sense of irresponsibility amongst the borrowing States.

The Centre has not used its fiscal dominance over the States to correct regional imbalances. Nor has the Centre used other instrumentalities at its disposal to narrow down the unevenness in regional development. In the absence of an integrated approach to the development of the backward regions the location of the central sector projects and the inducing of private industry through the licensing policy, developmental rebates, etc., have not created much of an impression on the problem of regional imbalances. The indications are that regional disparities have grown under the plans. Even, the network of banking and other financial institutions has only helped to transfer resources from the relatively poorer to the richer areas. It would thus appear that the existing fiscal arrangements may have to be basically altered with a view to bring about a substantial increase in the free resources of the States, to scale down the indebtedness to manageable proportions and to transfer adequate resources to the poorer States so that they may have enough elbow room to adjust their plans to suit their own peculiar circumstances and fill in the gaps in their development and to catch up with the more advanced States in the Union.

Such a drastic readjustment in the fiscal framework may not have been necessary if the buoyancy of state revenues arising from the tempo of development was sufficient to take care of the expanding commitments for infrastructure activities and social services. The existing arrangements seem to have assigned a more favourable tax base to the Centre. Under the existing scheme of distribution of tax powers relating to property, land constitutes the main base for State taxation, whereas taxation of industrial and commercial property is the preserve of the Centre. In a densely populated country the volume of land assessable to tax remains almost static. Therefore, land as a source of revenue would largely depend on enhanced rates on

the one hand and enlarged agricultural incomes on the other. In contrast, the step up in the pace of industrial development under the Plans has meant a tremendous expansion in the base of industrial and commercial property and the income and wealth arising therefrom. This seems to have given a buoyancy to the Central revenues which is not available to any tax head assigned to the States. Besides, the dominant resource position has enabled the Centre to make massive investments in large-scale industrial and commercial undertakings which have enormous revenue potential. In this respect the domain of the States could not extend far beyond the generation and supply of electricity, operation of road transport and so on.

No doubt, States where industrial and commercial activities are concentrated do enjoy a differential advantage over the others in respect of elasticity and buoyancy of their taxes especially in the case of commodity taxes. But commodity taxation is a field which is jointly being exploited by the Centre and the States. In this customs duties are a central prerogative. So are the excise duties except those levied on alcoholic liquor and narcotics. There is already a ceiling placed on the rates on inter-state sales. Some commodities subjected to additional excise duties in lieu of sales tax seem to be suffering from neglect. These restraints along with the need to move in harmony with the neighbouring States seem to give the Centre an edge over the States in commodity taxation. The scope for raising sizable revenue through registration, motor vehicles and other taxes is clearly limited. When viewed within these overall limits set by the fiscal framework obtaining today the performance of the State Governments in tax effort can by no means be regarded as small. In fact, many more constraints would become evident when we look at State taxation in the light of the Directive Principles of State Policy and the stated objectives of planned development in India.

Apart from certain generalised objectives such as the promotion of the welfare of the people and ensuring social and economic justice, the Directive Principles of State Policy have laid special emphasis on the need to secure the distribution of ownership and control of the material resources of the community to subserve the common good and to ensure that the operation

of the economic system does not result in the concentration of wealth and means of production to the common detriment. Despite the ambiguities associated with the interpretations of the terms 'welfare', 'social and economic justice' and 'common good' and so on, the twin objectives of economic policy enshrined in the Directive Principles of State Policy may be said to be:

(1) an equitable distribution of ownership and control of the material resources of the community; and

(2) the prevention of concentration of wealth and means of production resulting from the operation of the economic system.

These objectives are loudly echoed in the Plan documents. Though the accent of the Five Year Plans has been on increased production, rapid industrialisation with particular emphasis on the development of basic and heavy industries, expansion of employment opportunities and so on, the planners have assigned an important place to reduction of inter-personal and inter-regional inequalities. As partners in the national effort towards planned economic and social development, the State Governments may be said to be guided by the same objectives in the fulfilment of their responsibilities. In fact, these objectives are adequately reflected in our terms of reference. The tax policy of the Government of Kerala underlying the terms of reference may be briefly spelt out as:

(*a*) mobilisation of additional resources to meet the requirements of planned development;

(*b*) modification of the tax rates to ensure greater progressivity and equity;

(*c*) simplification and rationalisation of tax laws and tax structure;

(*d*) improvement of tax administration; and

(*e*) infusion of greater financial strength in local government.

It ought to be emphasised that the realisation of the broad social objectives outlined in the Constitution as well as in the Plan documents calls for a whole spectrum of policies designed

to change the structure of production, property relations and contractual payments as well as fiscal measures interfering with the process of income generation, the accrual of private and personal incomes and factors giving rise to disparities in standards of consumption. Only a simultaneous movement in all these directions would have facilitated the realisation of the stated goals and objectives. In other words, unless accompanied by some basic changes in the social and economic framework, fiscal measures will not be so effective in the realisation of our broad social goals and objectives.

Private property rights conferred by the Constitution constitute the major barrier to structural reforms. Powerful economic interests have been exerting pressures in favour of the *status quo*. But as mentioned earlier our heritage has been one of structural imbalances and gross social and economic inequities. Our socio-economic framework was such that agriculture and trade are almost entirely private. On the eve of planning, public ownership was restricted to a few economic and social infrastructures; the rest of industry was private. A few business houses dominated the corporate sector in industry, banking and wholesale business. Apart from feudal relations, ownership of land was concentrated in a few hands and the problem of tenancy and landless labour was acute. So far the pressure exerted by the propertied interests in favour of the *status quo* and the protection enjoyed by them under the Constitution seem to have succeeded in preventing basic changes in the property relations in land, industry and trade. In fact, the institutional and regulatory measures initiated under the Plans have hardly touched the fringe of the problems of inequality in income and wealth. There is reason to believe that the problems have been aggravated. Progressively inclined State Governments can do very little in dealing with these problems so long as the initiative for removal of the constitutional barriers rests with the Central legislature.

In an important sense taxation is a political process. As such, a tax system reflects the underlying economic and political interests. Tax legislation commonly derives from private pressures exerted for selfish ends. In a class ridden community those who feel the burden of taxation are naturally

prone to relieve themselves from their fiscal discomfort. One class struggles to throw the burden off its shoulders. If it succeeds, the burden must, of course, fall upon others. They also, in their turn, labour to get rid of it and finally the load falls upon those who will not or cannot make a successful effort for relief. Often, in this struggle, the rich only engage and the poor go to the wall! Thus class politics is the essence of taxation.

In the Indian situation the political pressures exerted by the already entrenched economic interests have put a powerful damper on the progressivity of the Indian tax structure. This is equally true of State taxation. The progressivity of a tax system is determined by the extent to which it conforms to ability to pay. And ability to pay is properly measured by income and wealth. Highly graduated income tax and death duties are regarded as ideal levies based on ability to pay. But these measures are repugnant to those who advocate the ideology of 'barriers and deterrents'. Their basic assumption is that Government is inherently wasteful. Therefore, they argue that income and death duties foolishly shift our economic resources from the thrifty ants to the irresponsible grasshopper! According to them, progressive taxes dangerously diminish the desire to work, fatally discourage the incentive to invest and irreparably impair the sources of new capital. It is also implicit in this argument that the greater the tax burden on the poor the harder they would work! A more sophisticated version of this line of thinking maintains that raising the savings ratio is the very essence of economic development and that a high rate of capital formation would depend on the extent to which consumption could be curbed and investment stimulated.

Since our planners are, by and large, persuaded by this outlook to economic development they have emphasised "the need for balancing the advantage of greater equality of incomes against the disadvantages of a possible fall in private savings and capital formation and general discouragement of production activities". In the absence of private property and striking income differential an overall curb on consumption to enlarge savings will not have serious social consequences. But in the context of wide economic disparities any such attempt to curb consumption

and subsidise investment would only tend to aggravate the problem of inequalities even when there is a growing public sector. The enormous increase in commodity taxation (both excises and sales taxes) coupled with heavy doses of deficit financing has had precisely this effect on the Indian economy. It follows that so long as the basic economic power structure interests remain undisturbed the ideology of barriers and deterrents will continue to plague state taxation. A simultaneous search for more resources and greater progressivity within the existing framework is beset with a lot of difficulties. The search for one is likely to endanger the pursuit of the other. For instance, any shift from the consumption-oriented to property or income-oriented tax structure may be conducive to greater progressivity in the system. But unless land-based taxes are made steeply progressive it is not likely to bring in a substantial increase in revenue.

The dilemma between increased production and equitable distribution of the burdens of resource mobilisation becomes more real when the State Governments assume the role of an underwriter of developmental efforts in their respective territorial jurisdictions. This has become all the more important in the hitherto industrially backward States where the local entrepreneurship has not been particularly aggressive. In their natural enthusiasm to get an edge over others in the race for development they are anxious to attract industries through tax inducements and stimulate production through subsidized inputs apart from providing the requisite infrastructure facilities. This is also true of subsidised social services which are sometimes rendered to the public irrespective of the differing abilities to pay, of the beneficiaries. But once people are used to a free or subsidised service it is only at grave political risk that the subsidy element could be withdrawn. In fact, the more widespread such services are, the greater is the political risk involved in the discontinuance of subsidies. By and large, the extra burden arising from these measures falls on the consuming masses of the population. As such the underwriter's or welfare approach to the development of the State economy or to public services tends to introduce an element of regressivity into the tax system.

As mentioned earlier, land is the main property base of the States. In most cases it is the major contributor to State (national) income. But its contribution to the State exchequer is relatively small. In an economic sense, mobilisation from agriculture (especially in the form of marketed surplus) depends on the productivity, crop pattern, relative prices, marketing facilities, procurement machinery and so on which are outside the scope of enquiry of this Committee.

Landed property confers several advantages on the owners. Apart from psychic income arising from power, prestige, security, and so on, land confers real economic advantages through income, rent, capital gains, etc. Part of this is unearned. Consequently the land owners stand on a privileged position vis-a-vis the large number of landless peasants, urban workers and even a large section of the salaried groups. In recent years non-agricultural lands in the urban areas, more than agricultural lands have registered an unprecedented appreciation in value on account of the rapid pace of urbanisation. Speculation in land has given a tremendous boost to land values. Considerable resources have flown into the urban sector by way of investment on land and other assets. On the other hand, land-use has become the crucial factor in town-planning. Mere taxation of land will, therefore, be far too inadequate in dealing with the complex problems of planned urban development. Only a carefully worked out programme of land nationalisation coupled with suitable measures of land taxation would provide the real answer to the problems created by speculative dealings and unplanned use of urban land.

As for land taxation the search is for a new basis which would combine the characteristics of productivity, equity, flexibility, progressivity and simplicity, and make land contribute its due to the State exchequer. Though simple, the basic tax of Kerala does not satisfy the other requirements. Land revenue based on cadastral surveys and settlement has proved to be regressive and static. But insofar as the results of capital improvements, infrastructure facilities and the pressure of population on land would be adequately reflected in the capital value of land, only this would offer a flexible basis for a progressive tax on land provided a machinery could be created

for periodic revision of the capital value of land.

If suitably designed, wealth tax, estate duty and succession duty on agricultural land may constitute a powerful instrument for raising revenues while reducing inequalities in agricultural property and wealth. But, so far, this group of taxes are hardly exploited. Though wealth tax as levied by the Centre on the assets of individuals and companies excludes agricultural land, the competence of the State Government to levy an analogous wealth tax on agricultural land is yet to be established. Succession duty, if levied, will arise only once every generation. But, so far, the State Governments have not paid enough attention to overcome the difficulties presented by Hindu undivided property. Estate duty on agricultural land also lacks prominence. Under the existing arrangements the Centre collects this duty and distributes the proceeds to the States after deducting collection charges. But the resources so raised are negligible in relation to the enormous stock of agricultural property. A determined effort in this direction would certainly bring in considerable revenue while at the same time narrow down the existing inequalities in the agricultural sector.

Agricultural income provides a facile base for progression in the rates of taxation, though most of the States have taken to it somewhat grudgingly. With appropriate differentiation in the rates between personal and company incomes on the one hand and domestic and foreign companies on the other, agricultural income tax could serve as one of the most progressive taxes in the fiscal kit of the State Governments.

Even in agricultural income the scope for substantial mobilisation is limited. Planning has been accompanied by several half-hearted attempts at changing land relations and ownership pattern. Abolition of intermediaries on land and imposing ceilings on land holdings have been the most significant of these reforms. Zamindari abolition resulted in a once-for-all increase in land revenue in the States affected by such reforms. On the other hand, ceilings legislation is an attempt to reduce the concentration of ownership in land and its redistribution amongst the landless poor. If successful it would have been one of the most progressive pieces of legislation introducing structural reforms in land ownership. Unfortunately, in most cases, it has not

produced surplus land on any significant scale for redistribution. On the other hand, large scale evasions (legal or otherwise) by way of distribution of holdings amongst members of the family have drastically reduced the scope for sizable increases in revenue through agricultural income tax except in the case of plantations and orchards where large sized holdings have definite commercial advantages. Insofar as such ceilings on size do not obtain in the industrial and commercial sectors, ceilings legislation on land may be said to have placed a serious constraint on resource mobilisation while at the same time it has not been so successful in redistributing land in favour of the poor.

Commodity taxation has become the predominant source of revenue in most of the States. In recent years it has also been enjoying an unusual buoyancy on account of the sharp increase in the general price level. It must be borne in mind that the net increase in revenue from such buoyancy related to price rise is hardly significant. Mostly a good part, if not the whole of the revenue effects of rising prices is neutralised by escalations in the cost of public services (Dearness Allowance increase is just one of them). In a sense, both these trends, higher prices and increased commodity taxation are indicative of the enormous burden of taxation shouldered by the less affluent sections of the population, for the bulk of the revenue from sales tax is from commodities of mass consumption. It is true that with the combination of single point with multipoint levies it has been possible to isolate articles of comforts and luxuries which are subjected to higher rates of duties. But since the volume of transactions in such commodities is small, the proceeds from these sources do not carry sufficient weight to make the system progressive. Theoretically there is no limit to the rate of tax on articles of conspicuous consumption. In fact, sales tax on liquors other than toddy is as high as 50 per cent in Kerala. But in this case temperance more than equity or yield is the dominant consideration. In other cases there are real constraints to imposing higher rates on luxury consumption. Some would argue that comforts and luxuries are in fact incentive goods and prohibitively high levies on them act as a deterrent on investment activities. For, according to them entrepreneurs save and invest so as to carry spendable profit which would give

them an advantage over others in conspicuous consumption. In many cases the real barrier in the way of higher taxes on luxuries is the fear of diversion of trade, smuggling and black marketing unless the concerned states move in step with their neighbours. Difficulties would arise when there is a substantial difference in the ideological quotient of the neighbouring Governments. In the absence of uniformity in the ideological outlook, regional councils in sales tax would only act as a curb on the progressive proclivities of the forward looking states.

Under these circumstances Governments inclined towards the strengthening of the progressive features of state taxation will have to resist the temptation for excessive tapping of commodities of mass consumption. Instead, they may have to enlarge the list exempting basic consumer goods and moderate the levies on others, while at the same time enhance the rates on luxuries and comforts. As indicated earlier, under the existing fiscal system, there are serious limitations in pursuing this without damaging revenue consideration. There may, however, be considerable room for improving the yield through simplification, rationalisation as well as by plugging the loopholes of evasion and avoidance. Recent years have also witnessed a considerable spurt in activities relating to the construction of residential buildings catering to the affluent sections of the population both in the rural and urban area. Suitable fiscal contraceptions may have to be devised to discourage such conspicuous consumption.

The scope for further increases in registration fees, stamp duties and taxes on motor vehicles appears somewhat limited. Logically, as part of the shift towards property-oriented taxes, there may be a case for enhancing the stamp duties arising from transactions in land and other immovable property. But the effect of any such enhancement may be lost unless effective measures are generated to counter attempts towards undervaluation of property . The proposed land tax on the basis of its capital value revised periodically would provide a firmer basis for checking such evasion. Much depends on how soon such an effective evaluation machinery could be brought into existence.

In recent years road transport has grown into a fairly big industry. It has become a necessary complement of industrial and agricultural development. As such the promotional element in the development of road transport is still kept alive. Though hardly any comprehensive data on the economics of road transport are available the general impression created by organised interests is that the burden of motor vehicles taxation and sales tax on motor spirits weighs too heavily on the industry. The proprietors of motor transport companies have been clamouring for improved roads on the one hand and reduced tax burden and enhanced fare structure on the other. It would, therefore, appear that apart from rationalisation and simplification the scope for enhancement of rates may be limited for some time to come. It may, however, be necessary to review the fees charged for the various services rendered by the Motor Vehicles Department by way of enforcement of the various regulations governing the operation of motor vehicles. However, one has to guard against possible attacks on the tax element in fees. In recent years, there has been a progressive advance towards nationalisation of bus transport. Over time nationalisation may be expected to embrace the entire passenger traffic on roads and even extend to the bulk of goods traffic. In that event, State Governments would be more concerned with the efficient and economic operation of the network of nationalised road transport than about enhancement of the rates of taxes on motor vehicles.

The role of the States as an underwriter and promoter seems to have constrained the tariff policy of the Electricity Boards in recent years. State Governments especially those with potential surplus of power seem to view with one another in selling power below cost so as to attract some of the heavily power using industries. In fact some of them (like Kerala) have entered into long term agreements with some bulk buyers. It is not so easy for the Electricity Boards to give up their promotional commitments in the near future. In any case, very little can be done by any particular Board so long as its counterparts in the neighbouring States persist with their policy of gravitating industries through attractive terms for the use of power. It is true that some differentiation in tariff is possible between essential and non-essential uses of power. But

if the Boards were to make profit it becomes necessary that the loss incurred on account of the subsidy element involved in the case of contractual buyers (large power using industries) can only be made good by throwing a relatively heavier burden on the mass of the consumers the bulk of whom belong to the middle classes. This is also true of the rapidly expanding rural electrification programme.

The problem of improving the yield from electricity has to be approached from several angles. If careful attention is paid to planning, feasibility study, detailed cost estimates, phasing and scheduling as well as the controlling of the progress of construction in terms of these cost estimates and work schedule, considerable savings would occur in the construction cost of power projects. Effective coordination between generation, transmission and sales promotion would also help to boost the operating receipts through near capacity utilisation. Stage by stage costing in terms of load factors may also be helpful in restructuring the tariffs on a more rational basis. Use of modern techniques of management such as materials management, management accounting and so on would help focussing attention on the most critical problems affecting costs. As for tariffs and duties most of the Boards seem to be committed to raising the return from electricity undertakings to 11 per cent of the capital base within an accepted time schedule. Yet it seems difficult for the Board to get away from the underwriter's approach.

Despite their promotional efforts most State Governments are unable to exploit the industrial potential unless private investors are aggressive enough or the Centre is impressed with the need for developing the potential. Consequently, the public sector undertakings are very few and relatively smaller in the scale of operation. Yet as in the case of electricity, if enough attention could be given to the problems of planning, programming construction and management of public undertakings they would add considerable resources by way of profits from public undertakings.

Kerala is one of the greatest foreign exchange earners in the country. Her products seem to enjoy an expanding world demand. In most cases the export sector is not properly

organised. Nor is it equipped to deal adequately with the whims of the world market. Under these circumstances organisation of marketing-boards or state trading in agricultural commodities may be expected to stimulate exports, while being highly profitable. Similarly, the prospect of planned development and use of the forest wealth as well as the development of forest based industries seem to be opening up attractive possibilities. The Plantation Corporation of Kerala only marks the beginning of progress in this direction.

As in Union-State Financial Relations the central problem in local finance is to ensure the purposeful matching of the need arising from the discharge of mandatory, discretionary and entrusted functions with resources providing at the same time for the fulfilment of national and regional priorities on the one hand and for a measure of local initiative on the other. The two-tier system of panchayati raj emerging in Kerala envisages further decentralisation of developmental and administrative functions and powers and the resources to discharge them. Strengthening the resource base of the local governments does not require constitutional changes except when the limit on profession tax is sought to be enhanced. It would, however, be necessary to take a fresh look at the taxes assigned to local bodies and review the basis of the tax sharing, grants-in-aid and loans available to them.

Though taxes are paid for the development of a civilized society, the tax-payer always feels deeply stung by the loss of money. The prevailing business ethics does not seem to jeer at tax avoidance and evasion. In fact some of the notorious tax delinquents occupy positions of power and responsibility in society. One of the biggest problems in tax administration is to develop an efficient machinery and procedures to deal with tax delinquents with a heavy hand while minimising the inconveniences to the honest tax payers.

To sum up, the tax potential in the States is not as great as it is sometimes imagined. The Constitution seems to have constrained State finances by placing certain expanding sources of revenues with the Centre and by extending undue protection to private property rights. But the Centre has not used its command over the direction of the overall resources at its

disposal towards balanced regional development. The existing fiscal arrangement may, therefore, have to be basically altered to leave enough initiative and resources with the weaker States to clear their backlog in development. Similarly, drastic changes in the property relations or income distribution would largely depend on the extent to which private property rights guaranteed under the Constitution could be curbed. The pressures exerted by the existing power structure account for the excessive reliance on commodity taxation and inflationary financing the brunt of the burden of which has been on the poorer sections of the population. The basic approach of a progressive tax policy should, therefore, be to shift the emphasis from a commodity based to a progressive and flexible group of taxes designed to tap more intensively land and the income and wealth arising therefrom. Secondly, to the extent that the role of the state as a promoter and an underwriter has tended to shift resources from the relatively poorer tax-payers to the affluent investors and producers, the policy of tax inducements and subsidies (hidden or open) may have to be carefully reviewed. But, both these approaches have severe limitations. The revenue potential of a really progressive structure of commodity taxation may be disappointing. On the other hand, where the pressure of population on land is great, the scope for mobilisation through graduated levies on land and agricultural incomes may not be impressive. At the same time, it would be difficult to ignore the role of the State as a promoter and underwriter of development so long as inter-state rivalries and the bargaining power of the investors remain as they are. It would, therefore, be wise to be selective and direct in dealing with subsidies. Thus, under the existing framework of economic and social relations even the most progressively inclined State Governments would be under severe strain if they were to ignore revenue and developmental considerations for the sake of progressivity.